95-1727

No. _____

Supreme Court, U.S.
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IN THE

Supreme Court of the United States

OCTOBER TERM, 1995

CAJUN ELECTRIC POWER COOPERATIVE, INC.,

Petitioner,

v.

CENTRAL LOUISIANA ELECTRIC COMPANY, INC., UNITED STATES OF AMERICA ON BEHALF OF RURAL UTILITIES SERVICE, DEPARTMENT OF AGRICULTURE, AND TECHE ELECTRIC COOPERATIVE, INC.,

Respondents.

On Petition for a Writ of Certiorari to the United States Court of Appeals for the Fifth Circuit

PETITION FOR A WRIT OF CERTIORARI

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April 22, 1996

QUESTIONS PRESENTED

1. Assuming *arguendo* that the existence of conflicts of interest may constitute "cause" for the appointment of a trustee pursuant to 11 U.S.C. § 1104(a)(1), may conflicts of interest that are *inherent* in a debtor's cooperative structure constitute such cause, when this creates a special cooperative-specific standard for the appointment of a trustee nowhere found in the Bankruptcy Code, contradicts Congress's expressed intent to encourage the cooperative structure for rural electric cooperatives, and creates a circuit split on an important matter of federal public policy?

2. In a reorganization case, may a bankruptcy court appoint a trustee for cause under 11 U.S.C. § 1104(a)(1), based only on the existence of conflicts of interest, when the Bankruptcy Code requires some parties—but not a debtor in possession—to be free from conflicts of interest, and when this Court has recognized a fundamental conflict of interest that *all* insolvent debtors in possession have?

3. May a bankruptcy court appoint a trustee for cause under 11 U.S.C. § 1104(a)(1), which provides that a trustee should be appointed only upon a showing of "fraud, dishonesty, incompetence, or gross mismanagement . . . by current management . . . or similar cause," where that court relies on the actions of third parties as justification for the trustee appointment, and where the record reveals no such "bad acts" by the debtor?

LIST OF PARTIES, PARENT COMPANIES AND SUBSIDIARIES

Parties

Cajun Electric Power Cooperative, Inc.
Louisiana Public Service Commission
Unsecured Creditors Committee
Members Committee
Western Fuels Association, Inc.
Triton Coal Company
Central Louisiana Electric Cooperative, Inc.
United States of America, on behalf of Rural Utilities Service, Department of Agriculture
Teche Electric Cooperative, Inc.
Gulf States Utilities Company
American Commercial Terminals
Burlington Northern Railroad Company
U.S. Trustee

The following are members of Cajun Electric Power Cooperative, Inc.:

Beauregard Electric Cooperative, Inc.
Claiborne Electric Cooperative, Inc.
Concordia Electric Cooperative, Inc.
Dixie Electric Membership Corporation
Jefferson Davis Electric Cooperative, Inc.
Northeast Louisiana Power Cooperative, Inc.
Pointe Coupee Electric Membership Corporation
South Louisiana Electric Cooperative Association
Southwest Louisiana Electric Membership Corporation
Teche Electric Cooperative, Inc.
Valley Electric Membership Corporation
Washington-St. Tammany Electric Cooperative, Inc.

Gulf States Utilities Company is a subsidiary of Entergy Corporation. The following are the other subsidiaries or affiliates of Entergy Corporation:

Arkansas Power & Light
Entergy Services, Inc.
Louisiana Power & Light Company
Mississippi Power & Light Co.
New Orleans Public Service Inc.
Systems Energy Resources, Inc.

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III. The court of appeals' holding that the mere presence of conflicts can justify the appointment of a trustee violates the plain language of the Bankruptcy Code and this Court's opinion in *Weintraub*. 9

IV. By affirming the appointment of a trustee without a finding that Cajun has engaged in ongoing bad acts of the type specified by § 1104(a)(1), and by relying on the actions of third parties as justification for a trustee appointment, the court of appeals violates the plain language of § 1104(a)(1) and congressional intent. 12

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RURAL UTILITIES SERVICE, DEPARTMENT OF AGRICULTURE,
AND TECHE ELECTRIC COOPERATIVE, INC.,
Respondents.

PETITION FOR A WRIT OF CERTIORARI TO THE
UNITED STATES COURT OF APPEALS
FOR THE FIFTH CIRCUIT

Cajun Electric Power Cooperative, Inc. ("Cajun"), respectfully petitions for a writ of certiorari to review the judgment of the United States Court of Appeals for the Fifth Circuit in this case.

OPINIONS BELOW

The order of the court of appeals denying Cajun's suggestion for rehearing en banc (App., *infra,* 24a) is unreported. The opinion of the court of appeals on panel rehearing (App., *infra,* 1a-2a) is reported at 74 F.3d 599 (5th Cir. 1996). The original opinion of the court of appeals (App., *infra,* 3a-14a) is reported at 69 F.3d 746 (5th Cir. 1995). The opinion of the district court (App., *infra,* 15a-22a) is unreported. The initial ruling of the district court (App., *infra,* 23a) is unreported.

JURISDICTION

The court of appeals entered its judgment on January 25, 1996. The jurisdiction of this Court is invoked under 28 U.S.C. § 1254(1).

STATUTES INVOLVED

Section 904 of the Rural Electrification Act of 1936, 7 U.S.C. § 904, provides that in making loans, the Administrator "Shall give preference to States, Territories, and subdivisions and agencies thereof, municipalities, peoples' utility districts and cooperative, nonprofit or limited dividend associations . . . "

Section § 1104(a)(1) of the United States Bankruptcy Code (the "Bankruptcy Code"), 11 U.S.C. § 1104(a)(1), provides in relevant part, that a trustee may be appointed in a case under Chapter 11 of the Code "for cause, including fraud, dishonesty, incompetence, or gross mismanagement of the affairs of the debtor by current management . . . or similar cause . . . "

STATEMENT OF THE CASE

A. Statement of Facts

Cajun is a rural electric power cooperative, owned by its twelve members and formed for the purpose of providing electricity to its members. In turn, Cajun's twelve members sell the electricity to their members, who total approximately one million retail customers in Louisiana. Cajun and its twelve members entered into long-term "all-requirements" contracts for the sale and purchase of that electricity. To provide that electricity, Cajun constructed power plants, and invested in a nuclear power plant constructed by another utility, using as financing loans or loan guarantees from the Rural Utilities Service (the "RUS"), pursuant to the Rural Electrification Act.

Congressional policy, as codified in the Rural Electrification Act, encourages the cooperative structure for rural power

companies because the Administrator of the RUS is required to give preference to cooperatives when making loans. *See* 7 U.S.C. § 904. In fact, all electric generation and transmission companies receiving loans from the RUS are organized as cooperatives. There are approximately forty such generation and transmission cooperatives throughout the rural areas of the United States serving millions of retail customers.

B. Proceedings Below

In December 1994, Cajun filed a petition for reorganization under Chapter 11 of the Bankruptcy Code. In April 1995, Respondents filed motions requesting the appointment of a trustee. The motions were opposed by Cajun, the Louisiana Public Service Commission (the "LPSC"), the Unsecured Creditors Committee, the Members Committee, and other creditors and parties in interest.

In May 1995, a Joint Stipulation of Facts (the "Joint Stipulation") was filed for use in connection with the motions. On August 1, 1995, the district court, sitting as a bankruptcy court, ordered the appointment of a chapter 11 trustee. (App., *infra,* 23a). Six days later, the district court issued its written opinion (the "Trustee Order"). (App., *infra,* 15a). Cajun timely appealed.

The Fifth Circuit put the matter down for expedited appeal. On November 20, 1995, a panel of the Fifth Circuit reversed and vacated the Trustee Order. (App., *infra,* 3a). On rehearing, the panel reversed its previous opinion and affirmed the Trustee Order. (App., *infra,* 1a). The mandate issued forthwith.

REASONS FOR GRANTING THE WRIT

I. Summary

The district court's Trustee Order and the court of appeals' affirmance on rehearing are based on the ground that several "conflicts of interest" constituted sufficient cause to justify the appointment of a trustee. Even if it is correct to say that the existence of a conflict of interest may justify the appointment of a

trustee, the courts below relied on the "existence and nature" of the all-requirements contracts between Cajun and its members, and certain rate related conflicts that are the inevitable result of the cooperative structure. Because several of the conflicts of interest relied on as "cause" for the appointment of a trustee are inherent in, or are a direct result of, Cajun's cooperative structure, the court of appeals impermissibly created a special rule for the appointment of a trustee in cases involving cooperatives. Such a special rule has no foundation in the Bankruptcy Code. The ruling of the court of appeals also contradicts Congress's expressed intent to encourage the cooperative structure for rural electric cooperatives, and creates a circuit split on an important matter of public policy.

The impact of the court of appeals' decision goes beyond its impact on cooperatives, and impacts all Chapter 11 debtors, because it holds that the mere presence of conflicts of interest can constitute cause for the appointment of a trustee. As this Court's decision in *C.F.T.C. v. Weintraub,* 471 U.S. 343 (1985), illustrates, certain conflicts of interest are present in every bankruptcy reorganization case. Bankruptcy is the forum where the conflicting interests of various creditor groups and the equity interests are to be sorted out. The existence of such conflicts is a *condition* common to any insolvent company in bankruptcy and therefore cannot be eradicated. *Conduct* of the debtor is the only basis to appoint a trustee under 11 U.S.C. § 1104(a)(1). The existence of a conflict of interest is not. Therefore, the mere presence of conflicts resulting from the debtor's corporate structure or financial condition, standing alone, cannot constitute cause for the appointment of a trustee.

The court of appeals' decision also impacts all Chapter 11 debtors, because it affirms the district court's appointment of a trustee absent a finding of pervasive and ongoing bad acts by the debtor's current management, or similar cause, as required by the plain language of the Bankruptcy Code in § 1104(a)(1) and congressional intent. In fact, the courts below relied on the actions of third parties to support the trustee appointment,

which, under the plain language of the Bankruptcy Code, cannot support the appointment of a trustee.

As each of these issues have dramatic and negative consequences far beyond the current dispute, it is appropriate for this Court to take certiorari to resolve these issues and provide guidance to the lower courts on these important issues of law and public policy.

II. By finding that the conflicts inherent in Cajun's cooperative structure can constitute cause for appointment of a trustee, the court of appeals improperly creates a special rule for cooperatives in bankruptcy, contradicts Congress's expressed intent to encourage the cooperative structure for rural electric cooperatives, and creates a circuit split on an important matter of public policy.

According to the National Cooperative Business Association, there are over 47,000 business cooperatives directly serving 40% of the American population. Business cooperatives include credit unions, insurance companies, rural utility cooperatives, agricultural marketing and supply cooperatives, heath care firms and other businesses. All of these diverse cooperatives, regardless of their size, function, or industry, share two fundamental characteristics—member ownership and sales primarily to their members.

Even if the existence of a conflict of interest is a valid ground for the appointment of a trustee under 11 U.S.C. § 1104(a)(1), at least three of the conflicts identified by the district court and the court of appeals as justifying the appointment of a trustee are inherent in, or directly arise from, Cajun's

structure as an electric cooperative.[1] One of them, the existence and nature of the all-requirements contracts, is at the core of what it means to be a cooperative. Therefore, it was an error of law for the district court and the court of appeals to rely on these factors as "cause" for the appointment of a trustee, because to do so creates a *per se* rule applicable only to cooperatives.

Under the holding of the court of appeals every cooperative would be vulnerable to the appointment of a trustee if it were to seek bankruptcy protection, simply because of its cooperative structure. There is simply nothing in the Bankruptcy Code that creates a distinct set of rules for cooperatives relative to all other forms of businesses.[2] In creating a special rule, the court of appeals has committed a critical and important mistake of law that will have disastrous consequences for any of the tens of thousands of cooperatives currently operating throughout the country who may need bankruptcy protection.

The court of appeals' decision, which prevents Cajun from operating as a debtor in possession because of its status as a cooperative, also contradicts the goals of federal law that

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[1] The factors relied on included the "nature and existence of all requirements" contracts, a dispute over an appeal of an LPSC order setting rates, and Cajun's failure to take a position in litigation between the RUS and the LPSC over which entity had the power to set Cajun's rates. The courts below also indentified other facts which are not as clearly linked to inherent conflicts arising from Cajun's cooperative structure, including actions by third parties. Because the court of appeals based its decision at least to some extent on the impermissible considerations, however, the case must be remanded for further consideration as to whether cause exists for appointing a trustee after these impermissible factors are eliminated from consideration.

[2] When Congress wished to restrict access to bankruptcy relief to a particular type of entity, it said so specifically. Congress provided specific rules in cases involving a "single asset real estate" business, *see* § 101(51B), § 362(d)(3), a "small business," *see* § 101(51C), § 1102(a)(3), § 1121(e), § 1125(f), a "family farmer," *see* § 101(18), and a "family farmer with regular annual income," § 101(19), among others. There are no such rules restricting a cooperative's access or rights under the Bankruptcy Code. The court of appeals decision creates one.

expressly encourage rural electricity providers to take a cooperative form. 7 U.S.C. § 904. Every electric generation and transmission company in the country that has received a loan from the RUS is organized as a cooperative. There are approximately forty generation and transmission cooperatives in the United States which, like Cajun, are owned by their members, and have all-requirements contracts with their members. Given that Congress has specifically encouraged Cajun and other rural electric cooperatives to organize themselves as cooperatives, the court of appeals should not create a new *per se* rule, nowhere justified by the language of the Bankruptcy Code, which punishes Cajun in its bankruptcy case for previously organizing as a cooperative. There is nothing in the Bankruptcy Code that permits the court to penalize Cajun for conducting business as a cooperative; and given Congress's express intent to encourage rural electric cooperatives, the court of appeals erred in doing so.

Moreover, the court of appeals' decision creates a circuit split with the Seventh Circuit's decision in *In re Wabash Valley Power Assoc., Inc.*, 72 F.3d 1305 (7th Cir. 1995), on this important issue of federal policy affecting millions of customers of electric power cooperatives throughout the country. In *Wabash,* the debtor was an electric cooperative chartered under Indiana law and the major creditor was the RUS. Cooperatives such as Cajun and Wabash differ from ordinary corporations in that, although the members own the cooperative, they receive no profit. *Wabash,* 72 F.3d at 1313. The primary benefit to members of an electric cooperative is the opportunity to purchase all needed electricity at favorable rates. The rates charged by electric cooperatives are regulated by state law. *Id.* at 1314. The advantageous federal lending rules and lack of profit for cooperatives should allow cooperatives to offer electricity to consumers at lower rates. *Id.*

In a cooperative, each member is both a participant in control of the cooperative and a customer of the cooperative. Under both roles, the members as owners have an incentive and

a fiduciary duty to keep rates low and to manage the organization according to the best interests of the population it is intended to serve, the members themselves as customers. *Id.* at 1319. Thus, it does not matter if an electric cooperative emerges from bankruptcy with the members still in control of the operation, still paying low rates, and still not paying off all creditors. *Id.* at 1318. "This outcome . . . is justified, even dictated, by [the] cooperative structure." *Id.*

Thus, in comparison to the Fifth Circuit's belief that the very existence and nature of the all-requirements contracts justified the appointment of a trustee, *Wabash* recognizes that the all-requirements contracts between an electric cooperative and its members *are the essence* of what it means to be an electric power cooperative, and stand as a justification for the reorganization plan that was confirmed in that case. *Wabash,* 72 F.3d at 1318.

The decisions in *Cajun* and *Wabash,* therefore, are in conflict on issues affecting billions of dollars to creditors and millions of rural electricity consumers. Moreover, these issues have now adequately percolated in the circuit courts. Rarely can a debtor, stripped of its property, take an appeal, making appellate guidance infrequent. The filing by Cajun commenced one of the largest bankruptcy cases in the nation, and the largest ever in the state of Louisiana. Cajun's structure is typical of a rural electric cooperative. Thus, while only two circuit courts have addressed this issue, identical issues will arise in every subsequent bankruptcy case involving a rural electric cooperative. Moreover, the reasoning underlying these cases will be applicable to any cooperative that files bankruptcy, regardless of industry. As any of these cases could affect millions of consumers and involve millions, if not billions, of dollars, the situation begs for resolution by this Court. Rural electric cooperatives are spread throughout the United States, thus this issue will not be contained by the Fifth and Seventh Circuits, but can be expected to arise in courts throughout the country in coming years. Given the creation of this new *per se* rule by the Fifth Circuit, cooperatives will have no

way of predicting their ability to continue as a debtor in possession, and thus they may be reluctant to attempt to invoke the protections offered by the Bankruptcy Code even if those protections are desperately needed. This Court should issue a writ of certiorari to review the Fifth Circuit's opinion and resolve this important circuit split.

III. The court of appeals' holding that the mere presence of conflicts can justify the appointment of a trustee violates the plain language of the Bankruptcy Code and this Court's opinion in *Weintraub*.

The Fifth Circuit's decision that conflicts of interest can justify the appointment of a trustee is contrary to the plain language of the Bankruptcy Code and this Court's opinion in *C.F.T.C. v. Weintraub*, 471 U.S. 343 (1985).

A debtor in possession is not required to be free of conflicts of interest. The Bankruptcy Code explicitly requires that certain parties in a bankruptcy case—but not the debtor in possession—cannot be allowed to have conflicts of interest. For example, the attorney for the debtor in possession must be disinterested, 11 U.S.C. § 327(a), and a trustee must be disinterested, 11 U.S.C. § 1104(b). Being "disinterested" means that a person does not hold or represent an interest materially adverse to the estate, its creditors, or its owners, 11 U.S.C. § 101(14)(E), *i.e.*, the person is free of any conflict of interest. The Bankruptcy Code never provides that a debtor in possession must be disinterested, or free from conflicts of interest.[3] When Congress drafted the Bankruptcy Code, Congress recognized the concept of conflict of interest, imposed on certain parties the requirement that they not have a conflict of interest, but recognized that it would not be appropriate to impose such a condition on debtors in possession.

This Court and several courts of appeals have recognized that debtors will have conflicts of interest. The *Weintraub* case

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[3] The Bankruptcy Code goes further, expressly refusing to impose certain duties on a debtor in possession, such as investigating the debtor's acts and conduct, that are imposed on a trustee, *see* 11 U.S.C. § 1107(a).

grappled with some of the consequences of the fundamental conflict that is present whenever a company is insolvent, or is on the verge of insolvency. Is the debtor's duty to shareholders extinguished because the creditors may have the primary, or sole, economic interest in the enterprise? Does the debtor in possession owe a primary duty to the creditors? *Weintraub* says no—the debtor's duties continue to all constituencies, and the debtor is to treat the various classes fairly, even though their interests may be directly in conflict. As this Court wrote in *Weintraub,* "[Respondents contend] the trustee's primary loyalty goes not to shareholders but to creditors . . . who often will be the only beneficiaries of his efforts. Thus, [Respondents] contend, as a practical matter bankruptcy trustees represent only the creditors. We are unpersuaded by this argument. First, the fiduciary duty of the trustee runs to shareholders as well as to creditors." *Weintraub,* 471 U.S. 354-55 (citations omitted). *"[I]f a debtor remains in possession . . . the debtor's directors bear essentially the same fiduciary obligation to creditors and shareholders as would the trustee . . . " Id.* at 355 (emphasis added). The obligation is "to treat all parties, not merely the shareholders, fairly." *Id.* at 356.

Decisions of the courts of appeals also recognize that specific conflicts of interest on the part of a debtor, or its directors, may exist in a bankruptcy case, and may require giving the creditor's committee power to take actions to protect the estate. *See, e.g., Louisiana World Exposition, Inc. v. Federal Insurance Co. (In re Louisiana World Exposition, Inc.),* 832 F.2d 1391 (5th Cir. 1987); *Creditors Committee v. Noyes (In re STN Enterprises),* 779 F.2d 901 (2d Cir. 1985).

The opinion below strikes out in a brand new direction. The Trustee Order and the court of appeals' affirmance fundamentally rewrite the Bankruptcy Code, by concluding that the existence of conflicts of interest can support the appointment of a trustee. This is contrary to the Bankruptcy Code and should be reviewed by this Court.

One of the underlying premises of the decisions below is that Cajun's overriding duty is to RUS and its other creditors, and Cajun should take any actions necessary to raise the rates charged the members under the all-requirements contracts. As noted above, this view was rejected in *Weintraub*. A debtor in bankruptcy must simultaneously balance its fiduciary duties to *all* of the parties in the case, and not just act on behalf of the creditors alone.

The courts below have postulated that Cajun cannot perform this duty because the members, as customers, want lower rates and because the members, as owners, control Cajun. The Seventh Circuit in *Wabash* recognized that it will be difficult for a debtor cooperative simultaneously to balance its fiduciary duties to all of these constituencies. *Wabash*, 72 F.3d at 1319. This tension, however, "is an inescapable product of the cooperative form." *Id.* Therefore, the debtor cannot be punished for exercising its fiduciary duty to its members even if this causes some difficulty for the RUS as a creditor. *Id.*

Determining that Cajun has a higher duty to creditors than it has to members violates the lesson of *Weintraub*. The Bankruptcy Code deals with the relative priority of creditors' claims and equity's interests in the context of what a plan of reorganization must provide in order to be confirmed. 11 U.S.C. § 1129. For the courts below to use the conflict between creditors and owners of a debtor as the basis for the appointment of a trustee simply misapprehends the issue posed by 11 U.S.C. § 1104(a)(1), and the role of a debtor in possession. The conflicting interests have not disappeared, but Cajun has been improperly dispossessed of possession of its estate. As the Fifth Circuit has committed a serious and important mistake of law with significant ramifications for the bankruptcy system as a whole, this Court should take certiorari to review this issue.

IV. By affirming the appointment of a trustee without a finding that Cajun has engaged in ongoing bad acts of the type specified by § 1104(a)(1), and by relying on the actions of third parties as justification for a trustee appointment, the court of appeals violates the plain language of § 1104(a)(1) and congressional intent.

By affirming the appointment of a trustee without a finding that Cajun has engaged in ongoing bad acts of the type specified by § 1104(a)(1), and relying on conduct of third parties as a justification to appoint a trustee, the court of appeals violates the plain language of § 1104(a)(1) and congressional intent, and commits an important error of law with broad and disastrous ramifications for the law and practice of bankruptcy.

The standards governing the appointment of a trustee are codified at 11 U.S.C. § 1104. Under § 1104(a)(1) a trustee is to be appointed "for cause, including fraud, dishonesty, incompetence, or gross mismanagement of the affairs of the debtor by current management . . . or similar cause . . . " A trustee may be appointed for cause only if one the enumerated requirements of § 1104(a)(1) is met. *See Billing v. Ravin, Greenberg & Zackin, P.A.*, 22 F.3d 1242, 1246 n.3 (3d Cir. 1994). What constitutes "similar cause" is an issue of first impression in this Court.[4]

The focus of 11 U.S.C. § 1104(a)(1) is plainly on actions of the debtor. Despite that, the court of appeals and the district court relied on the actions of *third parties* to justify the appointment of a trustee. One of the stipulated facts relied on by the court of appeals to justify the appointment of a trustee was that some of Cajun's members "expressed an interest in purchasing some of Cajun's assets." (App., *infra,* 13a). The court of appeals also relied on its conclusion that some of Cajun's members "were working at cross purposes" to justify the trustee appointment *Id.*

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[4] The district court justified its appointment of a trustee on both § 1104(a) and § 1104(a)(2). The court of appeal's opinion relies solely on § 1104(a)(1) and is silent with respect to subsection (2). Cajun will assume that the court of appeal's affirmance did not rest on subsection (2), and therefore subsection (2) is not at issue at this time.

Justifying the appointment of a trustee for Cajun by the actions of third parties is clear error, and should be reversed, to remind the lower courts of the importance of applying the plain meaning of the Bankruptcy Code.

In addition, there were no allegations and no findings in this case that Cajun was guilty of "fraud, dishonesty, incompetence or gross mismanagement" of Cajun's affairs. Therefore, under § 1104(a)(1), the district court had power to appoint a trustee only if Cajun's actions constituted *similar cause* to "fraud, dishonesty, incompetence, or gross mismanagement" of Cajun's affairs. Congress intended that the standard for appointment of a trustee under § 1104(a) would be high, and it specifically meant to reverse the "nearly absolute presumption" in favor appointing a trustee that had prevailed under the old Bankruptcy Act. *See* Bankruptcy Reform Act of 1978, House Committee on the Judiciary, House Report No. 95-595, 5 U.S.C.C.A.N. 5963, 6358, 95th Cong. 2d Sess. (1978). The legislative history reveals that the "court may order appointment [of a trustee] *only if* the protection afforded by a trustee is *needed* and the costs and expenses of a trustee would not be disproportionately higher than the value of the protection afforded." *Id.* (emphasis added). "The protection afforded by a trustee," the House Report continues, "would be needed, for example, in cases where the current management of the debtor has been fraudulent or dishonest, or has grossly mismanaged the company, or where the debtor's management has abandoned the business." *Id.*

Although few circuit courts have addressed the issue, Cajun has found *no* circuit court opinion affirming the appointment of a trustee absent specific findings of pervasive and ongoing "bad acts" harming the estate. *See, e.g., In re Sharon Steel,* 871 F.2d 1217 (3d Cir. 1989) (systematic siphoning of debtor's assets to

other companies under common control on eve of bankruptcy and continuing post petition gross mismanagement).[5]

The Fourth Circuit's opinion in *Dalkon Shield Claimants v. A.H. Robins Co., Inc.,* 828 F.2d 239 (4th Cir. 1987), is particularly instructive in construing § 1104(a)(1). In *Robins,* the court specifically made a finding that the debtor had violated an express prohibition combined in the Bankruptcy Code which was sufficient to warrant a civil contempt sanction. *Id.* at 241-42. Despite this specific finding of serious unlawful behavior by the debtor, the Court held that the bankruptcy court did not err in concluding that the debtor's improper conduct did not "rise[] to the level of 'cause'" sufficient to appoint a trustee. *Id.* The message of *Robins* is consistent with the plain language of § 1104(a)(1), which indicates that the legal standard for cause is extremely high and that the appointment of a trustee is appropriate only as a last resort when ongoing *misbehavior* by the debtor sufficiently harms the estate to "rise" to the level of cause. The existence of conflicts of interest, and the actions of third parties, simply cannot meet this test.

Finally, a trustee should be appointed only as a last resort when no other remedies are adequate. The legislative history notes that, "[g]enerally a trustee would not be needed in any case where the protection afforded by a trustee could equally be afforded by an examiner." *Id.* at 6358-59. The use of an examiner is encouraged as a means to "give the courts, debtors, creditors, and equity security holders greater flexibility in handling the

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[5] Unpublished circuit opinions also support Cajun's position. *see Fraidin v. Weitzman (In re Weitzman),* unpublished disposition 43 F.3d 1466, 1994 WL 687306 (4th Cir. Dec. 9, 1994), at *2 (affirming appointment of trustee where bankruptcy court found that debtor "had engaged in prolonged pattern of dishonest conduct"); *Boineau's Inc. v. Boineau (In re Boineau's Inc.),* 956 F.2d 1162, 1992 WL 38142 (4th Cir. March 3, 1992) (affirming appointment of trustee when record was "replete" with "uncontradicted examples of gross mismanagement in the affairs of the debtor" and the record showed uncontradicted evidence of the debtor's management "squandering corporate assets, hiding corporate records, and wrecking the [debtor's] business").

affairs of an insolvent debtor, *permitting the court to tailor the remedy to the case." Id.* at 6359 (emphasis added). Thus, the standard for appointment of a trustee is extremely high and a trustee should be appointed only when all lesser remedies are insufficient. *See Hester v. NCNB Texas Nat'l Bank (In re Hester),* 899 F.2d 361, 367 (5th Cir. 1990) (before a trustee is appointed, the court should determine "whether the incompetence and mismanagement evidenced by the [acts at issue], in the management and direction of the entire case, rose to a level sufficient to warrant the appointment of a trustee. *Involved in that determination is a consideration whether lesser remedies would have sufficed."*) (emphasis added).

Parties opposing the appointment of a trustee in this case presented several less intrusive remedies to the district court that are more closely tailored to the harms to be prevented. Under § 1104(a)(1), the district court was required to consider these alternatives, but refused to do so. The district court did not consider any of these alternatives on the merits, and there has been no finding by any court in the case that any of these remedies would have been insufficient, or that a trustee was necessary because no other adequate alternatives were available.[6]

In enacting the Bankruptcy Code in 1978, Congress signaled a strong and express intent that the debtor should remain in possession of the estate throughout a bankruptcy case, unless guilty of egregious and ongoing misbehavior or gross mismanagement that harms or wastes the assets of the estate. In Chapter 11, "[i]t is settled that appointment of a trustee should be the

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[6] In fact, the district court refused to even consider on the merits the appointment of an examiner or any other less intrusive remedies, such as a court order directing Cajun to take specified actions or empowering the creditor' committee to act. The court summarily dismissed the request that alternative remedies be considered. The court framed the issue as "[i]t's either going to be a trustee, or not a trustee; it will not be an examiner . . . All that happens when you have examiners is, they take eight months to do something and then they come to the court and ask for a trustee, or whatever period of time they want. So, it's either going to be a trustee or not a trustee."

exception, rather than the rule." *In re Sharon Steel Corp.*, 871 F.2d 1217, 1225 (3d Cir. 1989).

In § 1104(a)(1) Congress enumerated the types of serious misbehavior necessary to justify the appointment of a trustee with its accompanying costs and disruptions. The court of appeal's decision undermines this carefully drafted statutory scheme by defining "similar cause" so broadly as to include actions of third parties, and the existence of conflicts of interest that have caused no harm or waste to the estate. Indeed, the Fifth Circuit now suggests that a trustee may be appointed if the debtor has taken any actions that a "healthy" company would not, (App., *infra*, 13a), or if the case is a "large and messy bankruptcy that promises to get worse." *Id.* By loosening the requirements for appointing a trustee far beyond the limits contemplated by Congress in drafting § 1104(a)(1), and including consideration of actions of third parties, the impact of the court of appeal's opinion extends beyond this case, significantly altering the fundamental principles of bankruptcy law and reorganization practice established by the Bankruptcy Code. Therefore, it is appropriate for this Court to issue a writ of certiorari to review the court of appeal's opinion.

CONCLUSION

For the reasons stated above, Petitioner respectfully prays that a writ of certiorari issue to review the decision of the Fifth Circuit in this case.

This 22nd day of April, 1996.

Respectfully submitted,

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APPENDIX A

Opinion and Judgment of the United States Court of Appeals on Rehearing

In the Matter of CAJUN ELECTRIC POWER COOPERATIVE, INC., Debtor.

CAJUN ELECTRIC POWER COOPERATIVE, INC. et al., Appellants,

V.

CENTRAL LOUISIANA ELECTRIC COOPERATIVE, INC. et al., Appellees.

No. 95-30760.

United States Court of Appeals,

Fifth Circuit.

Jan. 25, 1996.

William Hardy Patrick, III, William H. Patrick, Baton Rouge, LA, John C. Weitnauer, Richard Neal Batson, Alston & Bird, Atlanta, GA, for Cajun Elec. Power Co-op., Inc.

R. Patrick Vance, Jones, Walker, Waechter, Poitevent, Carrere & Denegre, New Orleans, LA, for American Commercial Terminals.

Richard E. Matheny, Gordon, Arata, McCollam & Duplantis, Baton Rouge, LA, Ewell E. Eagan, Jr. and C. Peck Hayne, Jr., Gordon, Arata, McCollam & Duplantis, New Orleans, LA, Alan C. Wolf, New Orleans, LA, for Central Louisiana Elec. Co-op., Inc.

Thomas Marx Bondy, William Ruth Kanter, U.S. Dept. of Justice, Civil Division Appellate Staff, Washington, DC, for U.S. on behalf of Rural Utilities Serv.

John S. Koppel, U.S. Dept. of Justice, Civ. Div., Washington, DC, for U.S. on behalf of Rural Utilities Serv. and U.S. Dept. of Agriculture.

Nicholas F. LaRocca, Jr., Morgan City, LA, for Teche Electric Cooperative, Inc.

Tom F. Phillips, Taylor, Porter, Brooks & Phillips, Baton Rouge, LA, David J. Messina, Taylor, Porter, Brooks & Phillips, New Orleans, LA, for Gulf States Utilities Co.

Appeals from the United States District Court for the Middle District of Louisiana.

ON PETITIONS FOR REHEARING AND SUGGESTIONS FOR REHEARING EN BANC

(Opinion November 20, 1995, 5th Cir., 1995, 69 F.3d 746).

Before REYNALDO G. GARZA, BARKSDALE and EMILIO M. GARZA, Circuit Judges.

ORDER OF THE COURT:

Taking the petitions suggesting rehearing en banc as petitions for rehearing, said petitions for rehearing are hereby GRANTED as follows:

"After re-reading the stipulation on file in this case, we find the conflicts of interest within the members of the Board of Cajun Electric Power Cooperative, Inc., to be such that the court below was correct in the appointment of a trustee. We therefore withdraw all of section IV of the prior opinion found at 69 F.3d 746 and we adopt the reasoning of the dissent in its place.

The appointment of a trustee is therefore AFFIRMED."

APPENDIX B

Original Opinion of the United States Court of Appeals

In the Matter of CAJUN ELECTRIC POWER COOPERATIVE, INC., Debtor, CAJUN ELECTRIC POWER COOPERATIVE, INC., et al., Appellants,

V.

CENTRAL LOUISIANA ELECTRIC COMPANY, INC., et al., Appellees.

No. 95-30760.

United States Court of Appeals,

Fifth Circuit.

Nov. 20, 1995.

William Hardy Patrick, III, Baton Rouge, LA, Richard Neal Batson, John C. Weitnauer, Alston & Bird, Atlanta, GA, for Cajun Electric Power Cooperative, Incorporated.

Richard E. Matheny, Gordon, Arata, McCollam & Duplantis, Baton Rouge, LA,

Ewell E. Eagan, Jr., C. Peck Hayne, Jr., Gordon, Arata, McCollam & Duplantis, New Orleans, LA, for Central Louisiana Elec. Coop., Inc.

John S. Koppel, William Ruth Kanter, United States Department of Justice, Civil Division, Washington, DC, for United States of America on behalf of Rural Utilities Service.

John S. Koppel, U.S. Dept. of Justice, Civil Div., Washington, D.C., for U.S. Department of Agriculture.

Nicholas F. LaRocca, Jr., Morgan City, LA, for Teche Electric Cooperative, Inc.

Tom F. Phillips, Taylor, Porter, Brooks & Phillips, Baton Rouge, LA, David J. Messina, Taylor, Porter, Brooks & Phillips, New Orleans, LA, for Gulf States Utilities Company.

Appeals from the United States District Court for the Middle District of Louisiana.

Before REYNALDO G. GARZA, BARKSDALE and EMILIO M. GARZA, Circuit Judges.

REYNALDO G. GARZA, Circuit Judge:

Appellants appeal from the appointment of a trustee in a Chapter 11 bankruptcy. For the reasons stated below, we vacate the appointment of a trustee and remand for further proceedings.

I.

BACKGROUND

This is an appeal from the district court's appointment of a trustee for Cajun Electric Power Cooperative, Inc. ("Cajun"). The district court appointed a trustee because it found that conflicts of interest existed among Cajun's board members, and because it felt that the appointment of a trustee would be in the best interest of all parties.

Cajun's financial problems can be traced back to its ill-fated investment in Gulf States Utilities' River Bend Nuclear Power Facility ("River Bend"). Cajun borrowed at least $1.6 billion from the Rural Utilities Service ("RUS"), an agency of the federal government, to invest in River Bend. The investment went sour, and Cajun has since sued Gulf States Utilities on the grounds that it was fraudulently induced to invest in River Bend.

Cajun's financial problems came to a head when the Louisiana Public Service Commission ("LPSC") ordered Cajun to lower its rates. Because it could not meet its debt obligations under the lower rates, Cajun filed for bankruptcy under Chapter 11 the same day that the rate decrease went into effect. The

conflicts among Cajun's board members became apparent when the board had to decide whether to appeal the LPSC's order to lower Cajun's rates. This decision was made difficult by the fact that Cajun's board members were managers or board members of its twelve member companies, who bought all of their electricity from Cajun. If they voted to appeal the rate decrease, they would be attempting to raise the price of electricity charged to the member-customers for which they worked. On the other hand, if the prices were lowered, it would be more difficult for Cajun to pay its debt obligations. Several board members resigned because of this conflict, but the board ultimately decided to appeal the rate decrease. The appeal, however, was not successful.

The RUS, along with some of Cajun's other creditors, moved for the appointment of a trustee. The district court granted this motion, finding that a trustee should be appointed because of the conflict of interest created by the fact that Cajun's board members owed duties of loyalty to Cajun, to Cajun's creditors, and to Cajun's member-customers. Cajun appeals from the appointment of a trustee.

II.

APPEALABILITY OF THE APPOINTMENT OF A TRUSTEE

We turn first to the issue of whether the appointment of a trustee is presently appealable. Because this is an appeal from a district court sitting in bankruptcy, our jurisdiction is governed by 28 U.S.C. § 291 ("Section 1291"). Section 1291 provides that this Court has "jurisdiction of appeals from final decisions of the district courts..." Thus, whether the district court's appointment of a trustee is appealable turns on whether it is viewed as a final order.

Normally, a final order is one that ends the litigation in the trial court. However, because of considerations unique to bankruptcy appeals—such as the protracted nature of bankruptcy

proceedings and the large number of parties interested in them—courts have applied liberalized rules of finality for bankruptcy appeals. The appellees, citing *Matter of Hawaii Corp.*,[1] argue that these liberalized rules apply only to appeals from a district court's review of a bankruptcy court's decision pursuant to 28 U.S.C. § 158(d) ("Section 158(d)"), not to appeals from a district court sitting in bankruptcy pursuant to Section 1291. Other circuits, however, have refused to follow *Matter of Hawaii Corp.* They "see no reason . . . for interpreting the word 'final' in [Section] 1291 differently from the way [they interpret] it in . . . Section 158(d)."[2] We too see no reason to apply different rules of finality for Section 1291 appeals, and will apply the same rules that we apply to Section 158(d) appeals.

Applying this liberalized concept of finality, we must now determine whether the appointment of a trustee in a Chapter 11 case is a final, appealable order. This is a question of first impression in this circuit. The only case in this circuit addressing the appealability of the appointment of a trustee, *In re Delta Services Industries,*[3] is inapplicable to the case at bar. *In re Delta Services Industries* held that the appointment of an interim trustee in a Chapter 7 case is not immediately appealable. However, that case involved an interim trustee, the appointment of which "constitutes only a preliminary step in [a debtor's] liquidation."[4] The case at bar, on the other hand, involves the appointment of a permanent trustee who is to negotiate a plan of reorganization.

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[1] 796 F.2d 1139, 1141-42 (9th Cir. 1986).

[2] *Tringali v. Hathaway Machinery Co.*, 796 F.2d 553, 558 (1st Cir. 1986). *Accord A.H. Robins Co. v. Piccinin*, 788 F.2d 994, 1009 (4th Cir.), *cert. denied*, 479 U.S. 876, 107 S.Ct. 251, 93 L.Ed.2d 177 (1986); *In re Amatex Corp.*, 755 F.2d 1034, 1039 (3rd Cir.1985); *In re UNR Industries, Inc.*, 725 F.2d 1111, 1115 (7th Cir. 1984).

[3] 782 F.2d 1267 (5th Cir. 1986).

[4] *Id.* at 1271.

Four other circuits have allowed appeals from the appointment of a trustee.[5] Of those four, the First Circuit gave the most convincing rationale for asserting appellate jurisdiction. First, it noted that the appointment of a trustee in a Chapter 11 case is "a decision of a significant and discrete dispute."[6] It then went on to state that:

> It seems plain that the decision of an appeal from the court's order [appointing a trustee] could not be meaningfully postponed until the end of the entire Chapter 11 proceeding. If an appeal were postponed until a plan of reorganization were confirmed, there would be no satisfactory way to vindicate the [debtor's rights].[7]

This rationale is well-reasoned. Without an immediate appeal, a debtor would have no effective relief from an erroneous appointment. The only option would be an appeal after a plan of reorganization was confirmed. By that time, the debtor would already have been out of possession for months, if not years, and the only relief would be to vacate the plan of reorganization and start new negotiations with creditors. An immediate appeal is a better option. Consequently, we hold that the appointment of a trustee in a Chapter 11 case is an immediately appealable final order.

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[5] See *In re Plaza de Diego Shopping Center, Inc.*, 911 F.2d 820 (1st Cir. 1990); *In re Sharon Steel Corp.*, 871 F.2d 1217 (3d Cir. 1989); *In re Oklahoma Refining Co.*, 838 F.2d 1133 (10th Cir. 1988); *Dalkon Shield Claimants v. A.H. Robins Co.*, 828 F.2d 239 (4th Cir. 1987); *Cf. In re Reid*, 773 F.2d 945 (7th Cir. 1985);(holding that the appointment of an interim trustee in a Chapter 11 case is immediately appealable). But see *Matter of Cash Currency Exchange, Inc.* 762 F.2d 542, 546 (7th Cir.), cert. denied, 474 U.S. 904, 106 S.Ct. 233, 88 L.Ed.2d 232 (1985) (holding that the appointment of a trustee in a Chapter 11 case is not immediately appealable).

[6] *In re Plaza de Diego Shopping Center, Inc.*, 911 F.2d at 826.

[7] *Id.*

III.

STANDING

The appellees challenge the appellants' standing to bring this appeal. Only one appellee, Central Louisiana Electric Company, Inc. ("CLECO"), actually challenges Cajun's standing.[8] CLECO argues that Cajun lacks standing because it is "hopelessly insolvent." To have standing to appeal a bankruptcy order, a party must show that it was "directly and adversely affected pecuniarily by" the order, or that the order diminished its property, increased its burdens or impaired its rights.[9] CLECO argues that Cajun is so insolvent that it lacks any hope of return under any reorganization, and is thus not adversely affected by the appointment of a trustee. CLECO's argument is without merit. When the trustee was appointed, Cajun lost all the rights it had as a debtor-in-possession, including the right to operate its business. Clearly, it was aggrieved by losing the right to run itself. Accordingly, we hold that Cajun has standing to prosecute this appeal.

Although the appellees questioned the standing of the other appellants, we will only address the issue of whether appellant Cajun has standing. Because we hold that Cajun has standing, we need not consider whether the other parties have standing. The other parties raise the same issue on appeal—the propriety of the appointment of the trustee—as Cajun. Thus, whether they have standing to prosecute this appeal is of no consequence; because Cajun has standing, we can decide whether the district court erred in appointing a trustee even if the other appellants do not.

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[8] The other appellees merely challenge the other appellants' standing; they do not challenge Cajun's standing.

[9] *In re El San Juan Hotel,* 809 F.2d 151, 154 (1st Cir. 1987). See *Rohm & Hass Texas, Inc. v. Ortiz Bros. Insulation, Inc.* 32 F.3d 205, 208 n. 18 (5th Cir. 1994)(noting that, to appeal a bankruptcy order, a party must show that it was aggrieved by that order).

IV.

THE APPOINTMENT OF A TRUSTEE

We now turn to the sole substantive issue in this appeal, whether the district court erred in appointing a trustee. The district court justified its appointment on two grounds: First, it held that there was cause to appoint a trustee under 11 U.S.C. § 1104(a)(1); and second, it held that the appointment of a trustee was in the best interest of the parties under 11 U.S.C. § 1104(a)(2). The district court's appointment of a trustee is reviewable only for abuse of discretion.[10] Our review of the record convinces us that the district court abused its discretion in appointing a trustee.

We will first review whether the appointment of the trustee can be justified under 11 U.S.C. § 1104(a)(1) ("Section 1104(a)(l)"). Section 1104(a)(1) provides that a court shall order the appointment of a trustee—

> for cause, including fraud, dishonesty, incompetence or gross mismanagement of the affairs of the debtor by current management, either before or after the commencement of the case, or similar cause . . .

The appointment of a trustee pursuant to Section 1104(a)(1) is an extraordinary remedy, and there is a strong presumption that the debtor should be permitted to remain in possession absent a showing of need for the appointment of a trustee.[11] The parties moving for the appointment of a trustee have the burden of proof, which they must meet by clear and convincing evidence.[12]

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[10] *In re Sharon Steel Corp.*, 871 F.2d at 1225-26; *Dalkon Shield Claimants*, 828 F.2d at 242.

[11] 5 LAWRENCE KING, COLLIER ON BANKRUPTCY § 1104.01[7][b](15th ed. 1995).

[12] *Id.*

The district court gave several reasons for appointing a trustee,[13] but they all stemmed from one conflict of interest: Cajun's inherent conflict between the interests of its member-customers, who want low rates, and those of its creditors, who want to raise rates.[14] However, because this inherent conflict results from Cajun's organizational structure—a structure that Congress encouraged it to adopt—the conflict is insufficient to justify the appointment of a trustee.

Congress intended that utilities which borrowed from the RUS be cooperatives. The Rural Electrification Act of 1936[15] is set up to favor cooperatives. Specifically, it provides that in making loans, the Administrator "shall give preference to . . .

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[13] The district court gave the following examples of conflicts: (1) a dispute over the appeal of a Louisiana Public Service Commission order setting rates; (2) failure to collect monies owned by its member-customers; (3) failure to allow members access to information and to participate in possible sales of Cajun's assets; (4) failure to take a position in litigation between the LPSC and the RUS over which entity had the power to regulate its rates; (5) the interests of some of Cajun's members in purchasing some of its assets; and (6) the existence and nature of the all-requirements contracts between Cajun and its member-customers.

[14] The dissent claims that two of the reasons given by the district court, the failure to collect monies owed by member-customers and the failure to allow members access to information and to participate in possible sales of Cajun's assets, show conflicts not present in a healthy cooperative. However, we do not think that these reasons constitute sufficient cause to justify the appointment of a trustee under Section 1104(a)(1). Cajun's accounts receivable owed by its member-customers were no greater during the bankruptcy than they were before the bankruptcy. This, Cajun is simply operating as it did before it declared bankruptcy; it is not attempting to keep money from its creditors by failing to collect accounts receivable from member-customers. Similarly, Cajun's failure to share information about possible asset sales with CLECO or Teche Electric Cooperative, Inc. ("Teche") do not constitute cause for the appointment of a trustee. CLECO is attempting to acquire Cajun's members, and Teche is effectively controlled by CLECO. A healthy cooperative is not obligated to share information about potential sales of its assets with companies that are seeking to acquire its members.

[15] 7 U.S.C. § 901 *et seq.*

cooperative, nonprofit and limited dividend associations . . . "[16] In fact, according to the parties' stipulation in this case, all electric generation and transmission companies receiving loans from the RUS are organized as cooperatives. The fact that Congress and the RUS encouraged-if not required-Cajun to organize itself as a cooperative leads us to believe that any conflict inherently arising from Cajun's organization as a cooperative is insufficient to justify the appointment of a trustee. Further, holding that these inherent conflicts constitute cause for appointing a trustee would create a *per se* rule permitting the appointment of a trustee in any case involving a cooperative. Nothing in the Bankruptcy Code or its legislative history indicates that Congress intended such a *per se* rule. In fact, when Congress wanted to create special rules for certain types of businesses, it did so.[17] Congress did not create such a *per se* rule, and we refuse to create one by judicial fiat.

Because all of the conflicts found by the district court arose from Cajun's organizational structure, we hold that the district court erred in finding that cause existed to appoint a trustee.

Appellees cite *In re Colorado-Ute Electric Ass'n, Inc.*[18] for the proposition that the conflicts inherent in any cooperative justify the appointment of a trustee. That case, however, is distinguishable. In *Colorado-Ute,* the district court found that the debtor had committed a number of bad acts, including making transfers on the eve of bankruptcy in an effort to destroy the RUS' security interest, and that the debtor had an incompetent board and management. Cajun, on the other hand, has committed no such bad acts, and the district court did not find its management or board incompetent. Thus, the factors justifying

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[16] 7 U.S.C. § 904

[17] For example, Congress provided specific rules in cases involving "a single asset real estate business," *see* 11 U.S.C. §§ 101(51B), 362(d)(3), a "small business," *see* 11 U.S.C. §§ 101(51C), 1102(a)(3), 112(e), 1125(f), and a "family farmer," *see* 11 U.S.C. § 101(18), among others.

[18] 120 B.R. 164 (Bankr. D. Colo. 1990).

the appointment of a trustee in Colorado-Ute are not present in the instant case.[19]

The district court also justified its appointment of a trustee upon Section 1104(a)(2). That section provides that the district court shall appoint a trustee when such an appointment is in the best interests of all the parties. The district court found that the appointment of a trustee was in the best interests of the parties because of the conflicts discussed above. However, just as such conflicts do not justify the appointment of a trustee for cause pursuant to Section 1104(a)(1), they also do not make the appointment of a trustee in the best interests of the parties under Section 1104(a)(2).[20] Further, the fact that the debtor and several creditors are appealing the trustee's appointment is evidence that the appointment was not in their best interest.[21] Thus, we hold that the district court erred in finding that the appointment of a trustee was in the parties, best interests.

In closing, we note that our vacation of the appointment of the trustee does not leave the parties' best interests unprotected. The bankruptcy court, even with the debtor in possession, can still enter orders in the reorganization plan to be adopted and the lack of the trustee is not an impediment to this inherent power of the bankruptcy court.

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[19] The dissent claims that we would never affirm the appointment of a atrustee in a case involving a cooperative where the cause for appointment can be traced back to a cooperative's inherent structure. We disagree. In a case like *Colorado-Ute,* where a cooperative had actually engaged in bad acts, we would affirm the appointment of a trustee.

[20] *See* COLLIER ON BANKRUPTCY, *supra* note 11, at § 1104.01[7][d] (noting that "there are few situations . . . when grounds will exist for the appointment of a trustee under [Section 1104(a)(2)] although 'cause' for such appointment will not exist under [Section 1104(a)(1)].").

[21] *See* COLLIER ON BANKRUPTCY, *supra* note 11, at § 1104.01[7][d] (noting that "[i]n any case in which equity security holders or other ownership interests support the debtor's current management, the court should refrain from appoint a trustee under [Section 1104(a)(2)]").

V.

CONCLUSION

Because the district court erred in appointing a trustee, we VACATE the appointment of the trustee and REMAND this case for further proceedings.

EMILIO M. GARZA, Circuit Judge, concurring in part and dissenting in part: I concur in the majority opinion except as to Part IV and the ultimate judgment. I do not agree with the majority that affirming the district court's order would create a "*per se* rule" under which any cooperative seeking Chapter 11 protection would be automatically subject to the appointment of a trustee. In my view the conflicts present in this case provide sufficient "cause" to support the district court's appointment of a trustee under § 1104(a)(1). *See* slip op. at 749 n. 13 (detailing Cajun Electric's conflicts of interest). The conflicts present in this case go beyond the "inherent" conflicts under which all healthy cooperatives operate.[22] Presumably, healthy cooperatives do not fail to collect monies owed by member-customers or attempt to deny member-customers access to information. Nor do members in healthy cooperatives consider strategies which seem designed to break-up and scavenge the assets of the debtor. *See* Joint Stipulation at 4 ¶ 15 ("Some members . . . have expressed an interest in purchasing Cajun's assets, either by themselves alone or by forming a venture with one or more others."). Once cooperative members begin working at cross-purposes, to the extent Cajun's members have, the appointment of a trustee may be the only effective way to pursue reorganization. *See In re Colorado-Ute Electric Ass'n., Inc.*, 120 B.R. 164, 176 (D. Colo. 1990) (holding the appointment of a trustee

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[22] The majority also errs in conflating the conflicts "inherent" in any cooperative organization with those "arising from" inherent conflicts. *See* slip op. at 749. In my opinion, the majority would shield a cooperative from trustee appointment, no matter how egregious its internal conflicts were, so long as the conflicts could be traced back to the cooperative structure.

proper where court could not envision a way for current management to resolve conflicts). As the district court recognized, this is a large and messy bankruptcy that promises to get worse without a disinterested administrator at the helm. Accordingly, I respectfully dissent from Part IV of the majority opinion, and would affirm the district court's appointment of a trustee.

APPENDIX C

OPINION OF THE UNITED STATES DISTRICT COURT

UNITED STATES BANKRUPTCY COURT
MIDDLE DISTRICT OF LOUISIANA

IN RE: CASE NO. 94-11474

CAJUN ELECTRIC POWER COOPERATIVE, INC. CHAPTER 11

USDC NO. 94-CV-2763

DEBTOR

RULING ON MOTIONS FOR APPOINTMENT OF TRUSTEE

Motions have been filed by the United States, on behalf of the Rural Utilities Service ("RUS"), Central Louisiana Electric Company, Inc. ("CLECO") and Teche Electric Cooperative, Inc. ("TECHE"), requesting the Court to appoint a trustee pursuant to section 1104 of the Bankruptcy Code, 11 U.S.C. § 1104. Gulf States Utilities ("GSU") has filed a response in support of the motions. Cajun Electric Power Cooperative, Inc., ("Cajun") and other parties to the bankruptcy proceeding have filed oppositions.

After conducting oral argument on the motions, the Court took the matter under advisement. On August 1, 1995, the Court issued a brief ruling granting the motions to appoint the trustee. The Court now assigns written reasons for its decision.

I.

FACTUAL BACKGROUND[1]

Cajun filed a voluntary Chapter 11 bankruptcy petition in the United States Bankruptcy Court for the Middle District of Louisiana on December 21, 1994. Because of pending litigation involving Cajun and GSU,[2] this Court has presided in the bankruptcy case.

Cajun is a non-profit electric generating and transmission cooperative that is wholly owned by twelve non-profit retail electric distribution cooperatives. These electric distribution cooperatives are owned by their members, who are also consumers. Each of the electric distribution cooperatives have two representatives on Cajun's Board of Directors.

Relying on section 1104(a)(1) and (2), movers contend that a trustee should be appointed for cause and because it would be in the best interest of the creditors and the estate. The Court agrees.

II.

DISCUSSION

Under Chapter 11 of the Bankruptcy Code, a debtor-in-possession can remain in control of the business operations and retain management unless a party in interest can prove that the appointment of a trustee is warranted. Absent a need for the appointment of a trustee, there is a strong presumption that the debtor should be permitted to remain in possession. The party

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[1] The Court has recently written an opinion in this case which sets forth factual background in more detail. Cajun Elec. Power Coop., Inc., v. Lousiania Pub. Serv. Comm'n (*In Re Cajun Elec. Power Coop.*), No. 94-CV-2764 (M.D. La. July 20, 1995).

[2] Cajun Elec. Power Co=op. v. Gulf States Utils., C.A.No. 89-474. The Court has recetnly completed Phase I of this trial and now has the matter under advisement.

requesting the appointment of a trustee has the burden of proof to show either cause under section 1104(a)(1) or that it is in the interest of the creditors, equity security holders, and other interest of the estate under paragraph (a)(2).

A debtor-in-possession has all of the duties of a trustee in a Chapter 11 case, including the duty to protect and conserve property in its possession for the benefit of the creditors. A debtor-in-possession's fiduciary obligation to its creditors includes refraining from acting in a manner which could damage the estate or hinder a successful reorganization of the business. When a debtor-in-possession cannot perform these duties, a Chapter 11 trustee should be appointed.

Cause exists under section 1104(a)(1) when the debtor engages in conduct such as fraud, dishonesty, incompetence, gross mismanagement, or similar cause. It is clear that the grounds for cause are not limited to those enumerated in section 1104(a)(1). Cause can consist of other factors, including an actual conflict of interest. If the Court determines that cause exists under section 1104(a)(1), the Court shall order the appointment of a trustee.

Even if there is no cause, a Court may appoint a trustee under section 1104(a)(2) if it is in the best interest of creditors or of the estate. Under this section, there is a flexible standard for the Court to follow. In determining whether to appoint a trustee under section 1104(a)(2) the Court may consider: (1) the trustworthiness of the debtor; (2) the debtor-in-possession's past and present performance and prospects for the debtor's rehabilitation; (3) the confidence or lack thereof of the business community and of creditors in present management; and (4) the benefits derived by the appointment of a trustee, balanced against the cost of the appointment.

The Court may appoint a trustee at any time after the commencement of the case provided it is done before the confirmation of a plan.

While the Court believes the burden is on the movant to prove the need for the appointment of a trustee by clear and convincing evidence,[3] the Court believes the evidence in this case satisfies this standard. It is clear from the facts of this case that there is cause to appoint a trustee because of the actual conflict Cajun has in this case between Cajun and its members, Cajun and the estate, and Cajun and its creditors. In short, the many conflicts of interest that Cajun's management, directors and members have with each other and with their creditors and the estate mandates that there be a trustee appointed to operate the estate in a fair and impartial manner. This is particularly true under the facts of this case where millions of consumers will be affected by the debtor's actions or inactions. Furthermore, because Cajun owes the RUS in excess of $4 billion, the taxpayers of the United States have a right to have the debtor's estate managed in such a way that as much of the debt as possible can be paid rather than just written off. It is not necessary that the estate be guilty of fraud or dishonesty for the Court to find cause under section 1104(a)(1).

The actual conflicts in this case are numerous. The potential for more conflicts in the future is inevitable under the facts of this case. The memorandums filed by RUS, TECHE, and CLECO spell out these conflicts in detail. Some will be summarized here.

There is a strong dispute between some individual members of the debtor over whether there should be an appeal of the decision of the Louisiana Public Service Commission which ordered Cajun and its members to reduce their rates. Some members of the board even resigned because they recognized the conflict. Different positions have been taken by some members on the appeal. Some want the board's decision to be reversed to lower the rates even more, while some want the commission's decision to lower rates to be reversed. There is little doubt that the lower the rates charged, the less revenue

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[3] *In Re* Sharon Steel Corp., 871 F.2d 1217, 1226 (3rd Cir. 1989); *In Re* bellevue Place Assocs., 171 B.R. 615, 623 (Bankr. N.D. Ill. 1994).

there will be to pay the outstanding debt in this case. Furthermore, any rate increase which Cajun might seek is adverse to its members. The Court does not believe that it should delay the appointment of a trustee to allow Cajun's management, directors and members to resolve their individual disputes at the expense of the creditors and the debtor's estate. Under the facts of this case, it is impossible for the debtor-in-possession to act as a fiduciary for the estate at the same time as it acts as a fiduciary for its members and customers. And, as noted earlier, because of the number of consumers involved and the potential loss to the taxpayers of this country, it is important that a neutral person oversee the debtor-in-possession to avoid any appearance of impropriety in this case.

There are other examples of conflicts: failure to collect moneys owed by the member cooperatives; failure to allow some members access to information about and to participate in possible sales of the debtor's assets; the manner in which the All-Requirements Contracts between Cajun and its members operate, which causes conflicts of interest between the officers and directors of Cajun, the interlocking directors and officers, and the member cooperatives; Cajun's failure to take a position on the preemption issue which was recently decided by the Court; the interest of some members in the purchase of all or part of the debtor's estate, and their apparent desire to be able to purchase the property at the lowest price possible; the conflict which may arise because of the members' interest in purchasing part of the estate in determining whether to accept or reject other offers which may be made; and the apparent primary interest of the Cajun board in protecting the rates and the actual existence of its members rather than trying to maximize the value of the debtor's estate. In short, the Court finds that the debtor-in-possession is impaired in its ability to reorganize itself because of the actual conflicts it has.

Decisions rendered by two courts in similar suits support the Court's decision in this case. In *Wabash Valley Power Ass'n v.*

Rural Electrification Administration,[4] the Seventh Circuit in a case involving electric cooperatives noted:[5]

> [Cajun] is operating as a debtor-in-possession. A debtor in bankruptcy is supposed to maximize the value of the estate, which opposition to a rate increase does not. Th[ese two] suit[s] by these four RECs and the motion to dismiss Cajun's appeal for a rate increase] serv[e]the interest of [Cajun]'s members at the expense of the interest of [Cajun]'s creditors . . . [Cajun should not be] allowed to operate as debtor-in-possession, when the clash of interests between creditors and its current management is so obvious.[6]

In *In Re Colorado-Ute Electric Association, Inc.,*[7] the court found that the inherent conflict of interest between the debtor, its members and creditors necessitates the appointment of a trustee.

For the same reasons set forth above, the Court finds that it is in the interest of Cajun's creditors and estate that a trustee be appointed under section 1104(a)(2). The Court believes that it is absolutely necessary under the facts of this case that a neutral trustee be appointed to preside in an objective and impartial manner to bring this case to a swift and successful conclusion. As the court noted in *Colorado-Ute,* "serious conflicts . . . between and among the debtor, its board and creditors [made] the prospect for gridlock seem more probable than the ability to rehabilitate the debtor."[8] Such is the case now before the Court. There are millions of consumers and even more taxpayers who are directly affected by the outcome in this case. There is no

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[4] 903 F.2d 445 (7th Cir. 1990).

[5] This Court is substituting Cajun for Wabash in the Seventh Circuit's opinion.

[6] Wabash Valley Power Ass'n v. Rural Electification Admin., 903 F.2d at 451.

[7] 120 B.R. 164 (D. Colo. 1990).

[8] *Colorado-Ute,* 120 B.R. at 176.

further need for confusion, uncertainty or delay in this case. A trustee will able to ensure that a fair plan of reorganization will be submitted to the Court, serve as a liaison with the many regulatory agencies that are involved, objectively review the proposed sale of assets, and participate in settlement discussions in those cases in which Cajun is a party.[9] In short, the appointment of a trustee will serve the interest of the creditors, the equity interest holders, and the estate.

The Court finds that the following arguments made by Cajun and the other parties which oppose the appointment of a trustee have no basis in fact or law:

(1) A trustee cannot assume and assign the All-Requirements Contracts;[10]

(2) Cajun "could" incur tax liabilities if a trustee is appointed because it is possible that the appointment of a trustee will result in a loss of cooperative status for federal and state tax purposes and in a change of ownership for federal tax purposes;

(3) The cost of the trustee outweighs any benefit that the estate will receive;[11]

---

[9] This Court has recently taken under advisement phase I of the litigation between GSU and Cajun involving the River Bend Nuclear Plant. Depending on the Cort's decision, there will be a need for further litigation in this case. This case if very complex and has been very costly to the parties.

[10] It is clear that Cajun's obligations under these contracts do not require a special skill or qualification, nor does these contracts impose a strictly personal obligation on Cajun. In fact, Cajun's members receive much of their power directly from CLECO, GSU, and others under interconnection agreements.

[11] the Court realizes that the appointment of a trustee will require the expenditure of funds. However, the Court believes that theh appointment of a trustee will allow this case to be brought to a speedy resolution, while at the same time protect all of the parties involved. This Court intends to closely monitor the costs and fees incurred by the trustee in this case. If necessary, the Court intends to reduce the amount and fees and cost whre the facts warrant. In the final analysis, there will be no fair resolution of this case without theh assistance of a trustee.

(4) The election procedures for a trustee will involve more litigation.[12]

If ever there was a need for a trustee in a Chapter 11 case, this is one. The Court recognizes the impact the appointment of a trustee has in a bankruptcy case. However, in this case, there is not only cause to appoint a trustee, it is also in the best interest of the creditors, the equity interest holders and the estate. The appointment of a trustee will also give confidence to the millions of consumers and taxpayers who are directly and indirectly affected-by this bankruptcy case.

The United States Trustee shall submit a trustee to the Court for approval in accordance with law.

Baton Rouge, Louisiana, August 4, 1995.

FRANK J. POLOZOLA
UNITED STATES DISTRICT JUDGE

[12] The parties have agreed on a trustee after being ordered by the Court to meet with the United States Trustee. A motion to appoint a trusttee agreed to by the parties is pending before the Court.

APPENDIX D

ORDER OF THE UNITED STATES DISTRICT COURT

UNITED STATES DISTRICT COURT
MIDDLE DISTRICT OF LOUISIANA

IN RE:	CIVIL ACTION NUMBER 94-2763-B-2
CAJUN ELECTRIC POWER COOPERATIVE, INC.	CHAPTER 11
FEDERAL TAX ID NO. 72-0655799	CASE NO. 94-11474
DEBTOR	

RULING

For more detailed reasons to be assigned at a later date, the Court finds that a Chapter 11 trustee should be appointed under the facts of this case. The Court has been advised that if the Court ordered a Chapter 11 trustee to be appointed, the parties had agreed upon a trustee.

Therefore,

IT IS ORDERED that within five (5) days the U.S. Trustee shall appoint a Chapter 11 trustee and submit the name of the candidate to the Court for final approval.

Baton Rouge, Louisiana, August 1, 1995.

FRANK J. POLOZOLA
UNITED STATES DISTRICT JUDGE

APPENDIX E

Denial of Suggestion for Rehearing En Banc

IN THE UNITED STATES COURT OF APPEALS
FOR THE FIFTH CIRCUIT

CASE NO. 95-30760

In The Matter Of: CAJUN ELECTRIC POWER COOPERATIVE, INCORPORATED

Debtor

CAJUN ELECTRIC POWER COOPERATIVE, INCORPORATED; TRITON COAL COMPANY; LOUISIANA PUBLIC SERVICE COMMISSION; MEMBERS COMMITTEE; WESTERN FUELS ASSOCIATION, INC.; THE OFFICIAL COMMITTEE OF UNSECURED CREDITORS; BURLINGTON NORTHERN RAILROAD COMPANY; AND AMERICAN COMMERCIAL TERMINALS, A DIVISION OF AMERICAN COMMERCIAL MARINE SERVICE COMPANY;

Appellants

V.

CENTRAL LOUISIANA ELECTRIC COOPERATIVE, INC.; UNITED STATES OF AMERICA ON BEHALF OF RURAL UTILITIES SERVICE, U.S. DEPARTMENT OF AGRICULTURE; TECHE ELECTRIC COOPERATIVE, INC.; GULF STATES UTILITIES COMPANY;

Appellees

Appeals from the United States District Court for the Middle District of Louisiana, Baton Rouge

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ON PETITION FOR REHEARING AND SUGGESTION FOR REHEARING EN BANC

(Opinion 01/25/96, 5 Cir., , F.3d)

(March 27, 1996)

Before REYNALDO G. GARZA, BARKSDALE, AND EMILIO M. GARZA,

Circuit Judges

PER CURIAM:

☒ The Petition for Rehearing is DENIED and no member of this panel nor judge in regular active service on the court having requested that the court be polled on rehearing En Banc, (FRAP and Local Rule 35) the suggestion for rehearing En Banc is also DENIED.

☐ The Petition for Rehearing is DENIED and the court having been polled at the request of one of the members of the court and a majority of the judges who are in regular active service not having voted in favor, (FRAP and Local Rule 35) the suggestion for Rehearing En Banc is also DENIED.

☐ A member of the court in active service having requested a poll on the reconsideration of this cause En Banc, and a majority of the judges in active service not having voted in favor, Rehearing En Banc is DENIED.

ENTERED FOR THE COURT:

REYNALDO G. GARZA
UNITED STATES CIRCUIT JUDGE

Supreme Court, U.S.
FILED
MAY 24 1996
CLERK

No. 95-1727

In The

Supreme Court of the United States

October Term, 1995

CAJUN ELECTRIC POWER COOPERATIVE, INC.,

Petitioner,

v.

CENTRAL LOUISIANA ELECTRIC COMPANY, INC., UNITED STATES OF AMERICA ON BEHALF OF RURAL UTILITIES SERVICE, DEPARTMENT OF AGRICULTURE, AND TECHE ELECTRIC COOPERATIVE, INC.,

Respondents.

Petition For Writ Of Certiorari To The United States Court Of Appeals For The Fifth Circuit

BRIEF IN OPPOSITION OF RESPONDENTS CENTRAL LOUISIANA ELECTRIC COMPANY, INC. AND TECHE ELECTRIC COOPERATIVE, INC.

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QUESTION PRESENTED

Whether the courts below abused their discretion in determining that this debtor's conflicts of interest, together with a pattern of conduct resolving those conflicts against the interests of the bankruptcy estate, constitute cause for the appointment of a trustee under 11 U.S.C. § 1104(a)(1) and 11 U.S.C. § 1104(a)(2).

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STATUTES:

11 U.S.C. § 1104(a)(1) ..... *passim*

11 U.S.C. § 1104(a)(2) ..... *passim*

11 U.S.C. §§ 702 and 703 ..... 10, 11

BRIEF IN OPPOSITION OF RESPONDENTS CENTRAL LOUISIANA ELECTRIC COMPANY, INC. AND TECHE ELECTRIC COOPERATIVE, INC.

Central Louisiana Electric Company, Inc. ("CLECO") and Teche Electric Cooperative, Inc. ("Teche"),[1] respectfully represent:

STATUTES INVOLVED

In addition to appointment of a trustee for cause under 11 U.S.C. § 1104(a)(1), § 1104(a)(2) provides in pertinent part that a trustee shall be appointed:

> . . . if such appointment is in the interests of the creditors, any equity security holders, and other interests of the estate,. . . .

STATEMENT OF THE CASE

A. STATEMENT OF FACTS

Cajun Electric Power Cooperative, Inc. ("Cajun") is a hopelessly insolvent electric power generation and transmission cooperative attempting to reorganize in bankruptcy. It is wholly owned by twelve non-profit retail electric distribution cooperatives. These electric distribution cooperatives are owned by their members, who are also consumers. Each electric distribution cooperative has two representatives on Cajun's board of directors. Cajun

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[1] Pursuant to Supreme Court Rule 29.6, CLECO and Teche state that each has no parent or subsidiary company.

has entered into long term all-requirements power contracts with its member cooperatives. Under these contracts, the member cooperatives are required to buy all of their power requirements from Cajun (to the extent of its capacity), and Cajun is obligated to sell the member cooperatives the power they need at Cajun's cost of production. The costs of constructing Cajun's generation and transmission assets were financed by loans from the Rural Utilities Service ("RUS"). At the time Cajun's bankruptcy petition was filed, its obligations to the RUS exceeded four billion dollars.

Actions taken by Cajun's board manifested conflicts of interest unrelated to Cajun's cooperative structure. First, from the end of November 1994 (i.e., the month before Cajun filed for bankruptcy), to the end of March 1995, Cajun let its overdue receivables from its members balloon from four and one-half million dollars to over fifteen and one-half million dollars. Second, several of Cajun's members who are represented on Cajun's board of directors expressed interest in purchasing Cajun's assets as part of the competitive bidding process Cajun was undertaking to develop its reorganization plan. These prospective purchasers/members intended to participate as bidders in an auction they controlled. Third, after Cajun filed for bankruptcy, but before the motion for appointment of a trustee was filed, Cajun's board attempted to restrict access to information from Smith Barney Inc. (the investment banker that Cajun sought to hire to oversee the bidding process for Cajun's assets) to Cajun's board members only. Fourth, against the advice of its own professionals, Cajun's board sought to thwart CLECO (a creditor whom Cajun had already identified as

a potential bidder) from participating in the Smith Barney sales process for its assets.

Cajun's board of directors took other actions inimical to the bankruptcy estate which were related to its cooperative structure. Cajun's rates are regulated by the Louisiana Public Service Commission ("LPSC"). In December 1994, the LPSC ordered a $30 million reduction in Cajun's wholesale power rates, the event which precipitated Cajun's bankruptcy filing. After a contentious board meeting in which a number of directors resigned rather than vote, Cajun's board voted to appeal the rate reduction upon the affirmative vote of only 7 of its 24 directors. Several of the resigning members (all of whom subsequently rejoined the board) cited conflicts of interest over the rate issue in their written reasons for resignation. Cajun also refused to participate, along with the RUS, in litigation concerning the ability of the RUS to pre-empt state regulation of Cajun's rates because the LPSC refused to allow rates for Cajun which would service its debts to the RUS. These two examples of Cajun's conduct clearly demonstrated that its interest in lower rates for its members predominated over its interest in its own solvency.

B. PROCEEDINGS BELOW

The proceedings below are adequately described in the petition. It should be noted, however, that the Fifth Circuit's decision to affirm the district court's appointment, vacate its original opinion, and adopt the reasoning of the dissent, was based on a more careful reading of the

lengthy stipulation of facts submitted by both parties (App. 2a).[2]

SUMMARY OF ARGUMENTS FOR DENYING WRIT

The district court appointed a trustee not merely because it found conflicts of interest inherent in the cooperative structure of Cajun, but because it found that conflicts of interest were affecting Cajun's conduct and were likely to affect its future conduct. Because its decision was fact-specific, the district court's ruling and Fifth Circuit's approval of that ruling do not in any manner create a special rule for the appointment of trustees in cases involving cooperatives. There is no "split in the circuits" on the issue, and the questions petitioners claim to be presented are not. Additionally, since Cajun's conduct was affected by its various conflicts of interest, petitioner's claim that the Fifth Circuit's holding permits the appointment of a trustee in cases involving a "mere presence of a conflict of interest" is inaccurate; the appellate decision holds that the presence of significant conflicts of interest and actions reflecting those conflicts of interest may constitute cause for the appointment of a trustee regardless of the legal structure of the debtor. That holding is nothing more than the application of plainly worded statutes to the facts of the case. Lastly, because the *conduct* of Cajun arose directly from the conflicts of interest with which the district court was concerned, the

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[2] References are made to the appendices attached to Cajun's Petition and cited "(App. ___a)."

district court and the Fifth Circuit reached the correct and proper conclusion: a trustee was necessary to protect the "best interests of the creditors" under § 1104(a)(2) and was justified under § 1104(a)(1).[3]

The district court did not appoint a trustee because of the actions of remote "third parties"; the trustee was appointed because of the actions of Cajun and those of its member/owners which resolved their conflicts of interest in favor of the members/owners and against the interests of the bankruptcy estate. The district court did not fail to consider the application of less intrusive remedies to this case; it considered such remedies and rejected them as inadequate.

There are no compelling reasons for a review of the decisions below by this Court.

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[3] Petitioners curiously argue in a footnote that the appeals court opinion relies solely on § 1104(a)(1) and is silent with respect to subsection (2). Petitioner then assumes away subsection (2). The appeals court did not limit its approval to subsection (1). In its rehearing, the appellate court clearly stated that the district court's appointment was correct:

> After re-reading the stipulation on file in this case, we find the conflicts of interest within the members of the Board of Cajun Electric Power Cooperative *to be such* that the *court below was correct* in the appointment of a trustee, (App. 2a). (emphasis added)

The district court relied on both § 1104(a)(1) and (a)(2). (App. 20a). Thus, both the district court and the court of appeal considered § 1104(a)(2) and its more flexible standard for the appointment of a trustee applicable to this case.

ARGUMENT

I. The district court's appointment of a trustee was based on an analysis of the facts of the case – the conflicts of interest to which this debtor was subject and the actions of this debtor which reflected those conflicts of interest – and, therefore, does not create a special rule for cooperatives in bankruptcy, does not contradict any congressional intent and does not create a circuit split.

The district court did not justify its appointment of a trustee on the sole basis of Cajun's "organizational structure" as a cooperative. In fact, both courts below found that the appointment was warranted based on several instances of questionable conduct on Cajun's part. Not every cooperative in bankruptcy, by virtue of its "structure" would engage in conduct similar to the acts of Cajun. Thus, the appointment had little to do with the inherent structure of cooperatives generally, and had everything to do with the conflicts of interest that were manifested in the specific acts of Cajun. The Fifth Circuit wrote:

> The conflicts present in this case go beyond the "inherent" conflicts under which all healthy cooperatives operate. Presumably, healthy cooperatives *do not fail to collect monies owed by member-customers* or attempt to *deny* member-customers access to information. Nor do members in healthy cooperatives consider strategies which seem designed to *break-up and scavenge the assets of the debtor*. Once cooperative members begin *working at cross-purposes*, to the extent Cajun's members have, the appointment of a

> trustee may be the only effective way to pursue reorganization.

(App. 13a) (emphasis added).

Therefore, the appellate court specifically found that the district court's appointment of a trustee was justified by at least four separate instances of conduct unrelated to the "cooperative structure" of Cajun. The district court also listed several conflicts that arose out of the conduct of Cajun's board members. The district court found that these conflicts included:

> [1] the failure to collect moneys owed by the member cooperatives; [2] failure to allow some members access to information about and to participate in possible sales of the debtor's assets; [3] Cajun's failure to take a position on the preemption issue which was recently decided by the Court; [4] the interest of some members in the purchase of all or part of the debtor's estate, and their apparent desire to be able to purchase the property at the lowest price possible; [5] the conflict which may arise because of the members' interest in purchasing part of the estate in determining whether to accept or reject other offers which may be made . . . .

(App. 19a) (numbers inserted).

Because both courts below found conflicts of interest manifested in various acts of Cajun's board and its directors, petitioner's argument that the appellate court opinion created a special rule for cooperatives in bankruptcy is meritless. The only rule that can be gleaned from the two opinions is the following fact-grounded one: if a cooperative in bankruptcy does as Cajun did – i.e., fails to

collect moneys from its members, becomes fractionalized and some of its constituents seek to make a bid for its assets while denying potential creditor/bidders access to information about possible sales of its assets, and works at cross-purposes in order to benefit its members – a trustee may be appointed under § 1104(a)(1) and § 1104(a)(2). In short, this case is no more than an illustrative and simple application of § 1104(a)(1) and § 1104(a)(2) to certain facts (i.e., Cajun's actions) in this case.[4] Therefore, it does not impact an important matter of public policy or federal law.

Because the appellate court did no more than approve the district court's application of § 1104(a)(1) and § 1104(a)(2) to the facts of this case, no federal goal is contradicted. Moreover, nothing in the Bankruptcy Code, the Rural Electrification Act ("REAct"), or any other statute suggests that electric cooperative debtors (with or without outstanding loans from the RUS) are subject to any different considerations than any other debtor for purposes of determining whether a trustee should be appointed under § 1104(a)(1) or § 1104(a)(2). As the original majority noted about the Bankruptcy Code, "when Congress wanted to create special rules for certain types of businesses, it did so." (App. 11a).

Similarly, nothing in the REAct remotely suggests that debtors with outstanding RUS loans are subject to special rules for when a trustee should be appointed and that such debtors may engage in conduct that under the

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[4] As pointed out by the court of appeals, the district court's appointment of a trustee is, therefore, reviewable only for an abuse of discretion. (App. 9a)

plain language of § 1104(a)(1) and § 1104(a)(2) would warrant the appointment of a trustee for an ordinary corporate debtor. The cooperative preference in the REAct – or the cooperative structure generally – in no way lessens the effect that Cajun's conflicts have on its estate and creditors or immunizes Cajun from the consequences of its actions. The dissent, which was ultimately adopted as the majority opinion, responded to the original incorrect decision as follows:

> The majority also errs in conflating the conflicts "inherent" in any cooperative organization with those "arising from" inherent conflicts. In my opinion, the majority would shield a cooperative from trustee appointment, no matter how egregious its internal conflicts were, so long as the conflicts could be traced back to the cooperative structure.

(App. 13a n.22).

In other words, where "cause" exists, it does not disappear merely because the RUS lent the debtor money or – more generally – because the debtor voluntarily chose to organize itself under one business form instead of another. Here, the acts of Cajun and its directors constituted "cause" for purposes of § 1104(a)(1) and § 1104(a)(2), and a trustee was properly appointed.

Indeed, petitioner admits that not all of the conflicts will necessarily exist in every bankruptcy involving an electric cooperative. In footnote 1 of the petition, petitioner admits that "[t]he courts below also identified other facts which are not as clearly linked to inherent conflicts arising from Cajun's cooperative structure. . . . "

(Petition for Writ of Certiorari ("Petition") at 6 n.1). However, petitioner implies throughout its petition that the appointment was based on the "mere" presence of conflicts of interest "inherent" in the cooperative structure of Cajun. By the petitioner's own admission, the courts did not appoint a trustee because of the mere "structural tensions" present in an electric cooperative.

Petitioner cites this Court's opinion in *C.F.T.C. v. Weintraub*, 471 U.S. 343 (1985) for the proposition that conflicts of interest should be tolerated in bankruptcy. However, conflicts of interest of the sort in this case – actions by the debtor's owners which favor themselves at the expense of the estate or other parties in interest – are simply not the sort of minor and inevitable conflicts that arguably should be permitted.[5] Indeed, petitioners quote an important passage from *Weintraub*: "[I]f a debtor remains in possession . . . the debtor's directors bear essentially the same fiduciary obligation to creditors and shareholders as would the trustee." *Id.* at 355. (Petition at 10). Because a trustee has the duty of being free of conflicts of interest with respect to the sale of property of the estate, under the *Weintraub* language cited by petitioner, so does the debtor in possession.[6] Additionally, by

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[5] CLECO maintains that conflicts of interest of the debtor, inherent or not, can be so profound as to constitute cause for appointment of a trustee and does not waive its right to so argue. However, it does not believe that that question need be addressed in this case by this Court. The actions of Cajun were sufficient cause to justify appointment of the trustee.

[6] Although the cooperative structure does not permit conflict-free possession by the debtor under all of the conflict restrictions imposed on the trustee (*see* 11 U.S.C. §§ 702 and

engaging in acts that favored its members both financially and in the prospective sale of its assets, Cajun's board and its directors inappropriately and grossly tipped the scales to unfairly favor the members *to the detriment of the creditors and other parties in interest*.[7] This sort of action is misconduct that justifies appointment of a trustee regardless of the organizational structure of the debtor. Therefore, the lower court decisions do not contradict any federal goal relating to electric cooperatives.

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703), clearly Cajun was obligated at the very minimum to prevent blatant and avoidable conflicts of interest regarding the information accessibility and bid evaluation. Because it failed to act fairly in the face of such conflicts, the lower courts found cause sufficient to justify appointment of a trustee.

[7] In the typical bankruptcy case, a debtor's shareholders or members have an interest in maximizing the estate's value, so that as high a residual equity interest in the debtor as possible will remain for their benefit after the creditors (who have higher priorities to the estate) are accounted for. Thus, for example, unlike here, members of an electric cooperative debtor whose total debt is well below the total value of its assets retain a strong economic incentive in seeing that the estate's value is maximized. Similarly, members in an agricultural cooperative, where growers join together to sell their crops to outside buyers, should be economically aligned with the cooperative's creditors in seeing that the cooperative sells its crops at the highest possible price. But this case does not fit that typical mold. Absent a miracle, there is no possibility of a residual equity interest for Cajun's members. Its scheduled debt exceeds the scheduled value of its assets by over two billion dollars. With no hope of recovering any equity interest in the bankruptcy estate, the economic interests of Cajun's members are served by lower electric power rates and bargain purchases of Cajun's assets, neither of which necessarily maximizes the value of Cajun's bankruptcy estate.

Petitioners reach to another electric cooperative bankruptcy case, *Matter of Wabash Valley Power Ass'n, Inc.*, 72 F.3d 1305 (7th Cir. 1995), in an attempt to tease out a conflict with the Fifth Circuit's decision in this case. The *Wabash* opinion had nothing to do with appointment of a trustee. Therefore, petitioner must resort to dicta in the *Wabash* opinion in its search for a circuit split. Specifically, petitioner cites several passages from *Wabash* that speak to the nature of an electric cooperative. On appeal in *Wabash* were several objections by the RUS to the confirmation of the plan of reorganization in that case. On appeal in this case, however, was the appointment of a trustee under § 1104(a)(1) and § 1104(a)(2). The Petitioner's only authority for its contention that there is a circuit split is taken out of context from the section of the *Wabash* opinion discussing the absolute priority rule and the requirement thereunder that a plan be "fair and equitable." The actual language petitioner attempts to import into the trustee context was as follows:

> The absolute priority rule is an aspect of the requirement that a plan be "fair and equitable." There is some appearance of unfairness in the Wabash Plan. Wabash's member distribution cooperatives, whose representatives approved the Marble Hill fiasco, emerge from bankruptcy in the driver's seat, still paying low rates, and still not paying off the REA's debt. This outcome, however, is justified, even dictated, by Wabash's cooperative structure. The Members, by controlling Wabash, control their own rates, making it possible for them to be served under

> the 40 year requirements contract, which are, in turn, Wabash's most valuable possession.

Id. at 1318.

That the *Wabash* court found that the cooperative structure affected the value of the plans of reorganization does not conflict with the Fifth Circuit's conclusion that conflicts of interest and a pattern of resolving those conflicts against the interests of the bankruptcy estate justify appointment of a trustee. The *Wabash* opinion is devoid of any reference to the standards that must be applied under § 1104(a)(1) and § 1104(a)(2) to appoint a trustee over a bankrupt cooperative. Indeed, in an earlier decision involving the same bankruptcy proceeding, *Wabash Valley Power v. Rural Electrictrification Admin.*, 903 F.2d 445 (7th Cir. 1990), the Seventh Circuit actually expressed concern that Wabash had been permitted to remain as debtor in possession in light of the conflicts of interest:

> A debtor in bankruptcy is supposed to maximize the value of the estate, which opposition to a rate increase does not. This suit serves the interests of Wabash's members at the expense of the interests of Wabash's creditors. *We are surprised that the bankruptcy judge has allowed Wabash to operate as debtor in possession, when the clash of interests between creditors and its current management is so obvious.*

Id. at 451 (emphasis added).

Additionally, assuming arguendo the "spirit" of *Wabash* may not be reconciled with that of the appellate decision in this case (and that that constitutes a "split" among the circuits on an important issue), the facts of the two are easily distinguished: The appointment of a

trustee in this matter was justified by the conduct of Cajun's board and its directors. Similar facts were not reported in *Wabash*. Therefore, there is no discernible split between the Seventh and Fifth Circuits on the matter of appointment of trustees under § 1104(a)(1) and § 1104(a)(2).

II. The lower courts did not punish Cajun for the "acts of third parties," and the district court did consider measures less intrusive than a trustee.

Petitioner complains that in scrutinizing Cajun's conduct, the courts below have somehow held Cajun responsible for the actions of "third parties." These so-called third parties were Cajun's member/owner/rate payers. While it can be argued that Cajun does not control the actions of its members, there is no argument but that its members controlled Cajun. This is the fundamental source of the intractable conflicts of interest here. The actions of Cajun's board were not those of owners preserving and protecting a bankruptcy estate and attempting to maximize its value. The actions of Cajun's board reflected their interests in lowering Cajun's wholesale power rates to benefit the members in their capacities as rate payers and in minimizing the value of Cajun's assets to benefit them in their capacities as potential purchasers of those assets. It is silly to claim that the conduct of Cajun's member/owners in their individual capacities cannot be used to determine whether cause exists to replace them with a trustee in their capacities as fiduciaries to Cajun's bankruptcy estate. In any event, the courts below did not rely exclusively on the actions of Cajun's member/owners in their individual capacities in

determining that cause existed for the appointment of a trustee. Most of the conduct described by the lower courts was that of Cajun itself.

Petitioner complains that the district court refused to consider the less intrusive remedy of appointment of an examiner in the case. In light of the conflicts of interest and conduct of Cajun, the district court, acknowledging the presumption against the appointment of a trustee, concluded that "[i]f ever there was a need for a trustee in a Chapter 11 case, this is one." (App. 22a) Therefore, it concluded that a trustee was necessary in this case and that an examiner simply would not do.

CONCLUSION

For the reasons set out above, this is not a case worthy of the Court's limited judicial resources and a writ of certiorari should not be issued.

Respectfully submitted,

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Supreme Court, U.S.
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No. 95-1727

In the Supreme Court of the United States

OCTOBER TERM, 1995

CAJUN ELECTRIC POWER COOPERATIVE, INC.,
PETITIONER

v.

CENTRAL LOUISIANA ELECTRIC COMPANY, INC., ET AL.

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FIFTH CIRCUIT

BRIEF FOR THE UNITED STATES IN OPPOSITION

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QUESTION PRESENTED

Whether the district court abused its discretion in concluding that the debtor's numerous conflicts of interest provided cause for the appointment of a bankruptcy trustee in this case.

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OPINIONS BELOW

The opinion of the court of appeals on rehearing (Pet. App. 1a-2a) is reported at 74 F.3d 599. The initial opinion of the court of appeals (Pet. App. 3a-14a) is reported at 69 F.3d 746. The opinion of the district court (Pet. App. 15a-22a) is reported at 191 B.R. 659.

JURISDICTION

The judgment of the court of appeals was entered on January 25, 1996. A petition for rehearing was denied on March 27, 1996. Pet. App. 24a-25a. The jurisdiction of this Court is invoked under 28 U.S.C. 1254(1).

STATEMENT

1. In a Chapter 11 bankruptcy matter, the district court may order the appointment of a trustee for "fraud, dishonesty, incompetence, or gross mismanagement of the affairs of the debtor by current management, * * * or similar cause." 11 U.S.C. 1104(a)(1). A trustee may also be appointed "if such appointment is in the interests of creditors, any equity security holders, and other interests of the estate." 11 U.S.C. 1104(a)(2). The court's appointment of a trustee is reviewable only for abuse of discretion. See Pet. App. 9a.

2. Petitioner is a rural electric cooperative, financed in large part by federal loans and guarantees extended under the Rural Electrification Act of 1936 (the RE Act), 7 U.S.C. 901 *et seq.* It generates and transmits electric power, which it sells at wholesale to its twelve members, each of which is a rural distribution cooperative that is also financed under the RE Act. The distribution cooperatives, in turn, provide power at retail to their own members, commercial and residential customers who are the ultimate consumers of the system's electricity. The federal financing arrangements require each distribution cooperative to buy all of its power from petitioner, and require petitioner to set rates high enough to enable it to repay its debts. Petitioner is wholly owned by its members, and its board of directors is made up of two representatives of each member. See Pet. App. 4a-5a, 16a; C.A. App., Vol. II, Tab 6, ¶¶ 1-2.

On December 16, 1994, the Louisiana Public Service Commission ordered petitioner to reduce its rates so as to exclude from its rate base losses it

suffered from its failed investment in a nuclear power plant. Under the lowered rates, petitioner could not satisfy its debt obligations. On December 21, 1994, therefore, petitioner filed for protection under Chapter 11 of the Bankruptcy Code. See Pet. App. 4a, 16a.

3. On April 19, 1995, the United States and other creditors holding in the aggregate more than 99% of petitioner's debt[1] filed a motion in district court seeking appointment of a trustee for cause and because it would be in the best interests of the bankruptcy estate. After oral argument and extensive briefing by all parties, the court concluded that there was cause to appoint a trustee based on the following instances (among others) of demonstrated conflicts of interest:

> (1) After the state commission directed petitioner to reduce its wholesale power rates, several members of petitioner's board of directors resigned, citing irreconcilable conflicts of interest, rather than vote on whether to appeal. Pet. App. 5a, 18a. If petitioner successfully appealed the commission's order, its rates would go up and its revenues would increase, thus enhancing the value of the bankruptcy estate; but, by the same token, petitioner's members—its customers—would have to pay more for their electricity. *Id.* at 5a, 18a-19a.[2]

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[1] Petitioner owes the federal government more than $4 billion. See Pet. App. 18a.

[2] Ultimately, petitioner determined to pursue the appeal. Pet. App. 5a. The court of appeals' initial opinion erroneously indicated that the rate appeal has been decided. *Ibid.* In fact, that appeal remains pending in the state courts.

(2) The United States has argued in the underlying bankruptcy proceedings that the state commission's rate order is invalid under the Supremacy Clause. The district court rejected that argument, and it is the subject of a separate proceeding in the court of appeals, No. 95-30941 (5th Cir.). Even though judicial acceptance of the government's contention would increase the value of the bankruptcy estate by increasing rates and raising revenues, petitioner declined to join the government's suit. See Pet. App. 19a.

(3) Some of petitioner's members expressed an interest in buying its assets. C.A. App., Vol. II, Tab 6, ¶ 15. Although the interests of the bankruptcy estate would be furthered by a higher sales price, the prospective buyers—who control petitioner—are interested in obtaining a lower price. In addition, petitioner's board sought to exclude other member entities from the bidding process, even though those entities might offer a higher price. See Pet. App. 19a.

(4) Amounts that petitioner was owed by its customer-members increased markedly in the period from the end of November, 1994, one month before petitioner filed for bankruptcy, to the end of March, 1995, shortly before the motion for the appointment of a trustee was filed. C.A. App., Vol. II, Tab 6, ¶ 34; Pet. App. 19a.

The court concluded that the conflicts of interest between petitioner and its members, among petitioner's members, between petitioner and the bankruptcy estate, and between petitioner and its creditors rendered it "impossible for [petitioner as] the

debtor-in-possession to act as a fiduciary for the estate at the same time as it acts as a fiduciary for its members and customers." Pet. App. 18a-19a. The court rejected petitioner's argument that Section 1104(a)(1) requires proof that "the estate [is] guilty of fraud or dishonesty," *id.* at 18a, observing that the statute authorizes appointment of a trustee upon a showing of "fraud, dishonesty, incompetence, gross mismanagement, *or similar cause*," *id.* at 17a (emphasis added).

The district court also found that, because of the conflicts manifested in this case, "the appointment of a trustee w[ould] serve the interest of the creditors, the equity interest holders, and the estate." Pet. App. 21a (citing 11 U.S.C. 1104(a)(2)).

4. A divided panel of the court of appeals reversed. Pet. App. 3a-14a. The majority did not question the district court's finding that conflicts of interest had manifested themselves in the bankruptcy proceedings. It reasoned, however, that the potential for such conflicts is "inherent" in the structure of customer-owned cooperatives, *id.* at 9a-12a, and held that actual conflicts of interest reflecting that "inherent" potential do not suffice to displace a cooperative as debtor-in-possession, *id.* at 10a.

Judge Emilio M. Garza dissented in relevant part. Pet. App. 13a-14a. In his view, the conflicts in this case went "beyond the 'inherent' conflicts under which all healthy cooperatives operate." *Id.* at 13a; see also *id.* at 14a ("As the district court recognized, this is a large and messy bankruptcy that promises to get worse without a disinterested administrator at the helm."). He criticized the majority for "conflating the conflicts 'inherent' in any cooperative organization with those 'arising from' inherent conflicts,"

and expressed concern that the majority's approach "would shield a cooperative from trustee appointment, no matter how egregious its internal conflicts were, so long as the conflicts could be traced back to the cooperative structure." *Id.* at 13a n.22.

5. The court of appeals panel granted the government's petition for rehearing, and issued a new opinion affirming the district court. Pet. App. 1a-2a. After "re-reading" the record, the court "f[ou]nd the conflicts of interest within the members of [petitioner's board] to be such that the [district court] was correct in the appointment of a trustee." *Id.* at 2a. The panel therefore withdrew its prior opinion and "adopt[ed] the reasoning of the dissent in its place." *Ibid.*

ARGUMENT

1. Petitioner observes (Pet. 4) that certain conflicts of interest inhere in every bankruptcy reorganization case, and argues (Pet. 9-11) that the court of appeals erred in holding that the "mere presence" of such inherent conflicts constitutes cause for appointment of a trustee under Section 1104(a)(1). That argument is based on a mischaracterization of the opinion below. The court of appeals recognized —as had the district court—that extreme conflicts of interest can pose a danger to the debtor's estate, its creditors, and its equity holders similar in nature to that posed by "fraud, dishonesty, incompetence, or gross mismanagement." Pet. App. 17a-18a. The court of appeals then concluded, based on the record, that this case presented particularly egregious conflicts of interest that went well beyond the tensions inherent in any cooperative organization, and that the conflicts of interest posed a substantial threat to

a successful reorganization. *Id.* at 13a-14a & n.22, 18a-19a.[3] The court's holding that the district court acted within its discretion in appointing a trustee in these particular circumstances does not conflict with any decision of this Court or of any other court of appeals.[4]

2. Contrary to petitioner's argument (Pet. 5-9), the court of appeals' conclusion that appointment of a trustee was warranted in this case does not amount to a per se rule that every bankruptcy involving a co-operative involves conflicts of interest that warrant the appointment of a trustee. As the district court

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[3] Contrary to petitioner's argument (Pet. 12-15), the lower courts' findings were not based on the conduct of unrelated third parties. To the extent that the appointment of a trustee for cause under Section 1104(a)(1) requires proof of "bad acts" by the debtor-in-possession (Pet. 12-13), a court would be remiss in ignoring the conduct of those who control the debtor-in-possession. The finding of "cause" in this case was based on numerous incidents in which conflicts of interest affecting petitioner's members—which control petitioner through their control of its board of directors—resulted in conduct by petitioner that was detrimental to the interests of the estate, its creditors, and other members. For example, not only did "some of [petitioner's] members 'express[] an interest in purchasing some of [petitioner's] assets,' " Pet. 12, but some members who expressed such an interest "consider[ed] strategies which seemed designed to break-up and scavenge [petitioner's] assets," and petitioner denied other member-customers access to information in connection therewith, Pet. App. 13a.

[4] The district court's appointment of a trustee may also be sustained on the strength of its alternative holding (Pet. App. 20a-21a) that the severe conflicts of interest demonstrated in this case warranted the appointment of a trustee under Section 1104(a)(2), "in the interests of creditors, any equity security holders, and other interests of the estate," a holding not challenged by petitioner.

noted, "[i]f ever there was a need for a trustee in a Chapter 11 case, this [wa]s one." Pet. App. 22a. The motion for appointment of a trustee and the district court's order granting that motion were based on an active pattern of conduct that advanced the interests of some of petitioner's members at the expense of the estate, its creditors, and other members. Such activity is simply improper—it is not "inherent" in petitioner's cooperative structure. As the court of appeals recognized, "[t]he conflicts present in this case go beyond the 'inherent' conflicts under which all healthy cooperatives operate. Presumably, healthy cooperatives do not fail to collect monies owed by member-customers or attempt to deny member-customers access to information. Nor do members in healthy cooperatives consider strategies which seem designed to break-up and scavenge the assets of the debtor." *Id.* at 13a (footnote omitted).[5]

3. There is no conflict between the decision of the court of appeals in this case and that of the Seventh Circuit in *In re Wabash Valley Power Ass'n*, 72 F.3d 1305 (1995). That case did not involve a motion for the appointment of a trustee. It concerned the bank-

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[5] Congress's desire to encourage and aid rural electric cooperatives (Pet. 6-7) is irrelevant to the question whether a court should appoint a trustee to replace a cooperative as debtor-in-possession, given a finding of cause. The requirements for appointment of a trustee are governed by Section 1104(a) of the Bankruptcy Code, which reflects Congress's judgment that, given cause, the appointment of a trustee advances the overall interests of the parties to the bankruptcy. To the extent that conflicts of interest in bankruptcy may manifest themselves with particular frequency when the debtor is an electric cooperative, Pet. 4-5, the RE Act evinces no preference—one way or the other—respecting the retention of a cooperative as a debtor-in-possession.

ruptcy court's confirmation of a reorganization plan submitted by a bankrupt rural electric cooperative. The primary issue was whether the plan satisfied the Bankruptcy Code's absolute priority rule, 11 U.S.C. 1129(b)(2)(B) (ii), which provides that any dissenting class of unsecured creditors must be paid in full before a junior claim or interest can receive or retain any property under a reorganization plan. See *Wabash*, 72 F.3d at 1313-1320.[6]

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[6] The other cases that petitioner relies upon are equally inapposite. The sole question presented in *Commodity Futures Trading Commission* v. *Weintraub*, 471 U.S. 343 (1985), was "whether the trustee of a corporation in bankruptcy has the power to waive the debtor corporation's attorney-client privilege with respect to communications that took place before the filing of the petition in bankruptcy." *Id.* at 345. In *Committee of Dalkon Shield Claimants* v. *A.H. Robins Co.*, 828 F.2d 239 (4th Cir. 1987), the district court denied a motion for appointment of a trustee after holding the debtor-in-possession in contempt for improperly paying pre-petition debts without the court's approval. *Id.* at 240. The court of appeals affirmed the denial, noting that trustee appointment matters are within the "discretionary authority" of the trial courts, *id.* at 242, and that the district court had made an express finding that the appointment of a trustee could impede reorganization, *id.* at 241.

CONCLUSION

The petition for a writ of certiorari should be denied.

Respectfully submitted.

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IN THE

Supreme Court of the United States

OCTOBER TERM, 1995

CAJUN ELECTRIC POWER COOPERATIVE, INC.,
Petitioner,

v.

CENTRAL LOUISIANA ELECTRIC COMPANY, INC.,
UNITED STATES OF AMERICA ON BEHALF OF
RURAL UTILITIES SERVICE, DEPARTMENT OF AGRICULTURE,
AND TECHE ELECTRIC COOPERATIVE, INC.,
Respondents.

On Petition for a Writ of Certiorari to the
United States Court of Appeals
for the Fifth Circuit

PETITIONER'S REPLY MEMORANDUM

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6 pp

In April 1996, Cajun Electric Power Cooperative, Inc., Petitioner ("Cajun"), filed a Petition for Writ of Certiorari to the United States Court of Appeals for the Fifth Circuit (the "Petition"), in this case, Case No. 95-1727. In response to Cajun's Petition, the United States, on behalf of the Rural Utilities Service, Department of Agriculture, filed a brief in opposition (the "United States' Brief"), and a joint response was filed by Central Louisiana Electric Company, Inc. and Teche Electric Cooperative, Inc. ("CLECO's Brief"). (The United States' Brief and CLECO's Brief hereinafter will be referred to collectively as the "Briefs in Opposition.") The Briefs in Opposition share several important errors that Cajun now brings before this Court. Both Briefs in Opposition erroneously suggest that the lower courts' decisions should be affirmed under the abuse of discretion standard, even though issues of law are reviewable *de novo*, and some of the factors relied upon below were erroneous as a matter of law. The Briefs in Opposition also incorrectly state that Cajun has not contested the appointment of a Trustee under 11 U.S.C. § 1104(a)(2), and that the decision can be affirmed on the alternative ground of § 1104(a)(2).

The Briefs in Opposition argue that even if the lower courts improperly relied on Cajun's inherent conflicts in appointing a trustee, there are sufficient independent factual grounds to justify the lower courts' decisions on an abuse of discretion standard. *See* United States' Brief at 7-8, CLECO's Brief at 6-9. This argument is incorrect for two reasons. First, it incorrectly applies an abuse of discretion standard to issues of law, which are reviewable *de novo*. Second, even if the decision is reviewable only for abuse of discretion, a legal error is *per se* an abuse of discretion.

The Briefs in Opposition assume that the standard of review in this case is purely for abuse of discretion. This is incorrect, because the statutory construction of 11 U.S.C.

§ 1104(a)(1)[1] and the definition of "similar cause" under § 1104(a)(1) are issues of law reviewable *de novo* by this Court. *Pierce v. Underwood*, 487 U.S. 552, 558 (1988). Thus, it is an issue of law whether "similar cause" for appointment of a trustee under § 1104(a)(1) requires "bad acts" on the part of the debtor's management, similar to "fraud, dishonesty, incompetence, or gross mismanagement." It is also an issue of law whether inherent conflicts that arise from Cajun's cooperative structure, a structure that Congress encouraged it to adopt, can constitute "similar cause" for appointment of a trustee. By contrast, the District Court's findings of fact are reviewable for clear error, and the Court's application of the legal standard of § 1104(a)(1) to the facts is reviewable for abuse of discretion. *Id.* The Briefs in Opposition confuse the legal issue of defining "similar cause" under § 1104(a)(1), which is reviewable *de novo*, with the application of this legal standard to the facts, which is reviewable for abuse of discretion.

Second, even if the lower courts were correct in reviewing the appointment of a trustee for abuse of discretion, errors of law are not protected by the abuse of discretion standard. "A district court by definition abuses its discretion when it makes an error of law." *Koon v. United States*, 64 U.S.L.W. 4512, 1996 WL 315800, slip op. at *13 (June 13, 1996); *see also Cooter & Gell v. Hartmarx Corp.*, 496 U.S. 384, 405 (1990). The finding of "cause" by the District Court and the Court of Appeals is based at least partially on inherent conflicts related to Cajun's status as an electric cooperative, including the existence and nature of the all requirements contracts and disputes regarding the rates charged by Cajun to its members. *See* Pet. App. at 13a (incorporating footnote 13 of original panel opinion summarizing District Court's discussion of factors supporting finding of cause for appointment of a trustee); Pet. App. at 19a (listing factors supporting finding of cause for appointing trustee, including "the

[1] 11 U.S.C. § 1104(a)(1) provides in pertinent part that the bankruptcy court may appoint a trustee "for cause, including fraud, dishonesty, incompetence, or gross mismanagement. . . or similar cause."

manner in which the All-Requirements Contracts between Cajun and its members operate" and disputes related to the rates Cajun charges to its members). These factors are inherent in Cajun's structure as a rural electricity cooperative, a business structure which Congress encouraged it to assume; therefore, the lower courts erred as a matter of law in finding that they provide cause for the appointment of a trustee. Because the lower courts' findings of cause rested at least in part on these impermissible considerations, their decisions are not protected by the abuse of discretion standard.

The Briefs in Opposition ignore the fact that the lower courts relied at least in part upon these impermissible factors, thereby suggesting that the decision to appoint a trustee was based only on considerations unrelated to Cajun's cooperative structure. *See* United States' Brief at 3-5 (omitting from summary of lower courts' findings that the existence and nature of all requirement contracts was a factor in finding cause for appointment of a trustee); CLECO's Brief at 7 (quoting District Court's enumeration of factors providing cause for appointment of trustee, but omitting District Court's reference to the all requirements contracts). The lower courts found cause to appoint a trustee when Cajun's inherent conflicts are considered; this is not equivalent to finding cause when the inherent conflicts are excluded from consideration. *See* CLECO's Brief at 10 (arguing that because some of the factors considered by the lower courts were appropriate, the inclusion of some inappropriate factors is irrelevant). The refusal of the Briefs in Opposition to admit that the lower courts relied at least in part on Cajun's inherent conflicts, and the selective quotation of passages from the lower courts' opinions to omit these references, does not change the reality that in finding cause to appoint a trustee the lower courts relied at least in part on Cajun's inherent conflicts. Because the lower courts committed legal error by considering improper factors in finding cause to appoint a trustee, this case should be remanded for further consideration as to whether cause remains after these factors are eliminated.

The Briefs in Opposition also state that the Fifth Circuit relied on § 1104(a)(2) in affirming the appointment of a trustee, CLECO's Brief at 5 n.3, and that Cajun has not challenged this holding, United States' Brief at 7 n.4. Both of these statements are incorrect and misleading.

CLECO's statement that the Fifth Circuit actually relied upon § 1104(a)(2) does not comport with a good-faith reading of the Fifth Circuit's opinion. Judge Emilio M. Garza's dissent, which was later incorporated as the majority opinion, does not mention or refer to subsection (a)(2). Pet. App. at 13a-14a. Indeed, the only mention of § 1104(a)(2) in either of the Fifth Circuit's opinions was the holding in the Court's original opinion, later withdrawn, that there were *not* grounds for appointment of a trustee under § 1104(a)(2). Pet. App. at 12a. The District Court did rely upon § 1104(a)(2) as alternative grounds to justify the appointment of a trustee, but the Fifth Circuit did not.

The position of the United States that Cajun has not challenged the appointment of a trustee on the alternative grounds of § 1104(a)(2) also lacks merit. Unlike CLECO, the United States does not claim that the Fifth Circuit silently relied upon subsection (a)(2) in affirming the District Court. Instead, the United States argues: (i) that Cajun has not contested the appointment of a trustee under § 1104(a)(2), and (ii) that § 1104(a)(2) provides alternative grounds for affirming the appointment of a trustee. Both steps in this syllogism lack merit. First, Cajun unquestionably contested the appointment of a trustee under § 1104(a)(2) in both the District Court and the Court of Appeals, and intends to do so if it becomes an issue in this proceeding; therefore, it is simply inaccurate to state that the District Court's ruling on this point has not been "challenged." Second, the United States admits that only the District Court, and not the Fifth Circuit, relied on § 1104(a)(2) in making its decision; therefore, Cajun is unable to understand how § 1104(a)(2) could provide alternative grounds for the Fifth

Circuit's opinion or how Cajun's failure to appeal the Fifth Circuit's "nonruling" on this issue to this Court could constitute a decision not to challenge the District Court's holding. As the Fifth Circuit did not rely on § 1104(a)(2), it is not properly before this Court and cannot provide an alternative basis for affirming the appointment of a trustee. If this Court nonetheless wishes to address the issue of whether the appointment of a trustee was warranted under § 1104(a)(2) as well, Cajun will be happy to brief the issue at the Court's request.

This 12th day of July, 1996.

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